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## Monterey, California



# THESIS

**AN ANALYSIS OF THE FEASIBILITY OF  
OUTSOURCING CONTRACT ADMINISTRATION  
FUNCTIONS WITHIN THE DEFENSE CONTRACT  
MANAGEMENT COMMAND**

by

**Douglas P. Porter**

**June 1998**

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OUTSOURCING CONTRACT ADMINISTRATION  
FUNCTIONS WITHIN THE DEFENSE CONTRACT  
MANAGEMENT COMMAND**

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Submitted in partial fulfillment  
of the requirements for the degree of

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from the

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## ABSTRACT

Secretary of Defense William Cohen announced on November 10, 1997 the Defense Reform Initiative (DRI) which essentially outlines a plan to mirror those business practices that American industry has successfully used to become leaner, more flexible and more competitive. The DRI calls for a reduction in DoD infrastructure by means of subjecting the positions of 120,000 civil-service personnel performing non-inherently Governmental functions to the competitive A-76 process with private firms and other Government agencies during the next five years.

The Defense Contract Management Command (DCMC) which provides central contract administration services to DoD customers, has not historically pursued outsourcing as a means to reduce costs. This thesis examines outsourcing through the A-76 process, its advantages, disadvantages and its feasibility, applicability and current use at DCMC.





## TABLE OF CONTENTS

I.	INTRODUCTION.....	1
	A. BACKGROUND.....	1
	B. RESEARCH OBJECTIVE.....	6
	C. RESEARCH QUESTIONS.....	7
	D. SCOPE.....	7
	E. ASSUMPTIONS.....	8
	F. METHODOLOGY.....	8
	G. ORGANIZATION OF THESIS.....	9
II.	INFRASTRUCTURE REDUCTION AND OUTSOURCING.....	11
	A. BACKGROUND.....	11
	B. FORCE INFRASTRUCTURE.....	12
	C. COMPETITION AND MARKET INFLUENCE.....	16
	D. INTRODUCING COMPETITION TO GOVERNMENT FUNCTIONS.....	18
	E. OUTSOURCING AND PRIVATIZATION.....	20
	F. ADVANTAGES OF OUTSOURCING.....	22
	G. DISADVANTAGES ASSOCIATED WITH OUTSOURCING.....	30
	H. SUMMARY OF CHAPTER.....	34
III.	CONTRACT ADMINISTRATION SERVICES AND INHERENTLY GOVERNMENTAL FUNCTIONS.....	37
	A. CONTRACT MANAGEMENT AND ADMINISTRATION SERVICES.....	37
	1. Goal of Contract Administration.....	37
	2. Contract Administration Functions.....	38

B.	DCMC MISSION AND ORGANIZATION.....	40
1.	DCMC Overview.....	40
2.	DCMC Staffing and Skills Requirements.....	43
C.	DETERMINING LEVEL OF DCMC OVERSIGHT AND STAFFING.....	46
D.	INHERENTLY GOVERNMENTAL FUNCTIONS.....	47
1.	Definition.....	47
2.	Functions Considered to be Inherently Governmental.....	49
3.	Functions Not Considered to be Inherently Governmental.....	50
4.	DCMC Functions Considered Inherently Governmental.....	51
IV.	OUTSOURCING CONTRACT ADMINISTRATION FUNCTIONS.....	53
A.	INTRODUCTION.....	53
B.	CURRENT OUTSOURCING EFFORTS AT DCMC.....	54
C.	CONTRACTOR SELF-OVERSIGHT.....	55
D.	OPINION ON OUTSOURCIBILITY OF DCMC FUNCTIONS.....	59
E.	COMMERCIAL CONTRACT ADMINISTRATION PRACTICES.....	60
F.	CONTRACT ADMINISTRATION AND COMPLIANCE APPROACHES IN OTHER GOVERNMENT AGENCIES.....	64
1.	Technical Compliance Designees.....	64
2.	Outsourcing Contract Administration to Commercial Firms .....	65
G.	MARKET RESEARCH RESULTS.....	66
V.	DATA ANALYSIS.....	69
A.	INFRASTRUCTURE.....	69
B.	BENEFITS OF OUTSOURCING.....	71

C. INHERENTLY GOVERNMENTAL FUNCTIONS OF DCMC.....	73
D. CONTRACTOR SELF-OVERSIGHT.....	75
E. SOURCES OF SUPPLY FOR CONTRACT ADMINISTRATION FUNCTIONS.....	76
VI. CONCLUSIONS AND RECOMMENDATIONS.....	77
A. SUMMARY OF RESEARCH.....	77
B. CONCLUSIONS.....	78
C. RECOMMENDATIONS.....	83
D. ANSWERS TO RESEARCH QUESTIONS.....	85
E. AREAS FOR FURTHER RESEARCH.....	91
APPENDIX: SURVEY QUESTIONS AND RESPONDENTS.....	95
LIST OF REFERENCES.....	99
INITIAL DISTRIBUTION LIST.....	103



## **I. INTRODUCTION**

### **A. BACKGROUND**

Since the end of Desert Storm in 1991, the Department of Defense (DoD) policy has been one of downsizing through base closure and privatization. Although stated U.S. policy is to have resources to fight two wars at once, many experts warn that the nation would have trouble fighting and winning only one war today -- due in part, to money spent on non-military roles at the expense of core military programs. The end of Desert Storm has seen the following reductions in the U.S. military:

- Defense spending has declined 24 percent, in constant dollars, and manpower has been cut 27 percent.
- In 1991 there were 18 Army divisions - compared to only 10 today.
- The Navy has reduced its inventory of ships by 34 percent.
- Air Force tactical squadrons have been cut 28 percent.
- The Army's capability to deploy forces has dropped 44 percent while the Navy's support ships -- critical for overseas operations -- have been cut 61 percent.

From running day-care centers to handling supplies, DoD is engaged in functions that can and should be privatized. According to former Defense Secretary Caspar Weinberger, DoD could achieve savings from cuts in non-combat and non-core programs. Weinberger pointed out that the only sectors of the defense budget that have grown since the Cold War has been for the Defense Logistics Agency (DLA), which handles warehousing, inventory control and the transportation of supplies, as well as contract administration services, and the Defense Finance and Accounting Service



(DFAS) which manages payroll and budget -- all functions which could be successfully privatized or outsourced.[Ref 1]

Outsourcing is one part of an entire suite of efficiency-oriented defense reform initiatives that DoD has implemented. This initiative is generating savings for modernization, improving readiness, improving warfighter support and improving quality of life.

Dr. Paul Kaminski, the Under Secretary of Defense for Acquisition and Technology has stated; “Competition drives best value, not simply outsourcing for the sake of outsourcing. If done correctly, outsourcing will not only save money, it will help DoD to be an organization that thrives on competition, innovation, responsiveness to changing needs, efficiency and reliability.” [Ref. 2]

The guiding principles of DoD reform have been three-fold: first to adopt the most efficient organizational structures and management practices; second, to adapt the best business practices of the private sector to our needs; third, to rely on competition and the private sector for more of our goods and non-core services. Per Kaminski, DoD activities can be outsourced:

- If in-house performance of that activity is not required to meet requirements.
- If a competitive commercial market exists for the activity.
- If outsourcing the activity results in best value for the Government.

As a result of approximately 2,000 OMB Circular A-76 competitions (this process will be discussed at length in Chapter II), between 1978 and 1994, Kaminski reports that DoD now outsources 25 percent of post/base operation budget, 34 percent of

depot maintenance, ten percent of accounting and finance, 70 percent of Army aviation training, 45 percent of surplus property disposal, and 33 percent of parts distribution. This represents a \$1.5 billion savings in annual operating costs.[Ref. 2]

Since the establishment of DoD by the National Security Act of 1947, there have been many attempts to reform and streamline the acquisition management process. The passage of the 1998 National Defense Authorization Act contained some significant reform measures. One of the more significant reform measures was the restructuring of the DoD acquisition organization and workforce, including a 25,000 civilian personnel cut by October 1, 1998. In a letter to Secretary of Defense, William Cohen, the House Committee on National Security states,

In this time of constrained defense budgets, we believe full implementation of section 912 is a prudent step to eliminate unnecessary overhead costs and redirect resources urgently needed to offset modernization, readiness, and quality of life shortfalls.[Ref 3]

This workforce reduction measure has directly impacted the Defense Contract Management Command (DCMC). DCMC provides contract management services for DoD around the world throughout the acquisition lifecycle. As an organization, DCMC has 14,490 full-time employees, employed at 81 Contract Administration offices around the world. Currently, DCMC administers over 350,000 prime contracts, valued at over \$111 billion. [Ref. 4] Some of the DCMC core functions as specified in the Federal Acquisition Regulation (FAR) include:

- Price/ cost analysis
- Product quality assurance

- Contractor System Reviews
- Support to fact-finding and negotiations
- Safety and environmental assurance
- Control of Government-furnished property
- Management of transportation and packaging

Commanders of DCMC are currently faced with the challenge of achieving a 25 percent workforce reduction by the end of FY1998. [Ref. 3] If the reduction is not met through attrition, then a reduction in force may be necessary.

Prior to the 1998 National Defense Authorization Act, DCMC had been systematically reducing its workforce on a straight-line basis by approximately five percent per year since 1990. However, DCMC's workload has not been reduced by the same percentage. In the same timeframe, 1990 to 1997, DCMC has seen the average number of contracts requiring oversight decrease by only approximately 2.3 percent annually. [Ref 4]

In 1994 the Deputy Under Secretary of Defense (Acquisition Reform) directed that a cross-functional process action team (PAT) be formed to include representatives from the Office of the Secretary of Defense (OSD), the Military Departments and the DCMC. The PAT was to develop a specific plan of action to describe current inefficiencies in the DoD contract administration process and provide recommendations to resolve those inefficiencies through aggressive acquisition reform initiatives. The PAT was comprised of appropriate representatives to ensure a broad acquisition perspective. The PAT's purpose was to develop a comprehensive plan to reengineer specific elements

of the contract administration process within DoD to make it more efficient and effective, while achieving the following general goals. [Ref. 5]

- Reduce the time it takes to accomplish contract administration tasks (cycle time).
- Balance the need for a particular policy or procedure to protect or further a Government interest with the need for efficiency and cost savings, and with the need to innovate, and to manage risk rather than avoid it.
- Eliminate non-value added activities.
- Analyze current practices that are determined by the PAT to be candidates for reform.
- Identify costs (money, time, performance, personnel) associated with the practices.
- Identify "interested or affected parties" and consult with them about the practices, alternative approaches, preferred solutions, etc.
- Identify alternative approaches that are consistent with the current laws and supportive of the goals of the Charter.

The PAT's report presented 36 recommendations and 105 specific tasks to implement those recommendations.[Ref. 6] Some of the specific recommendations were:

- a. Tailored contract administration services: DoD contract administration oversight should be tailored based on a uniform risk assessment methodology.
- b. Alternative oversight proposals (AOPs): DoD activities should encourage and facilitate contractor preparation and submission of AOPs.

AOPs provide contractors with an opportunity to develop worthwhile alternatives to traditional Government oversight.

c. Contractor self-oversight: DoD should establish pilot locations to test the viability of contractor self-oversight through the use of technical compliance designees.

d. Major reengineering of the current CAS function of pre-award surveys is recommended to take advantage of other less costly and more timely ways to accomplish this function.

It was the consensus of the PAT that frequently DCMC engineers and functional specialists do not have the capabilities to perform needed surveillance. It recommended that innovative approaches to satisfy customer needs for contract administration be institutionalized. Noticeably absent from the PAT's findings was any recommendation to outsource any or all of the DCMC functions. Nor was outsourcing listed as a potential topic for future study.[Ref 6]

## **B. RESEARCH OBJECTIVE**

The objective of this study is to determine the feasibility of outsourcing DCMC functions. The researcher will define "privatization" and "outsourcing" and attempt to identify the specific DCMC functions that are "inherently governmental." The researcher will determine which DCMC functions are "outsourcable" according to the criteria set forth in current guidance. Market research will be conducted to identify potential commercial suppliers for these DCMC functions. The researcher will not attempt to perform a cost/ benefit analysis of outsourcing contract administration services but the research will lead to a recommendation for or against a formal A-76 cost study.



## **C. RESEARCH QUESTIONS**

The Primary Research Question is: **Can the Contract Administration functions performed by DCMC field offices be differentiated so as to identify those functions that can be outsourced?**

The following are subsidiary research questions:

1. What is “outsourcing” and “privatization”?
2. What is the process for determining if a function should or can be outsourced?
3. What are the advantages and disadvantages of outsourcing?
4. What are “inherently Governmental functions”?
5. What functions currently performed by DCMC fit the definition of “inherently governmental”?
6. Does DCMC currently subject their functions or personnel to the competitive A-76 process or have they in the past?
7. Do other Government agencies outsource CA functions?
8. Are there commercial suppliers for any or all of the DCMC functions?

## **D. SCOPE**

The scope of the thesis is to provide objective assessment to DCMC, both at the headquarters and field levels, as to whether outsourcing is an efficient and effective option in meeting their mission in the face of resource constraints, namely mandated downsizing. The study will include: (1) a discussion of outsourcing -- its purpose, advantages and disadvantages and current guidance on outsourcing Government functions, (2) an in-depth review of the mission and functions performed by DCMC, (3) a

discussion and definition of the concept of “inherently governmental” functions and analysis of which of the DCMC functions fit this definition, (4) a discussion of current guidance on outsourcing contract administration functions, (5) results of preliminary market research into a source for contract administration services, and (6) recommendations for or against DCMC pursuing an A-76 study.

## **E. ASSUMPTIONS**

This thesis is written with the following assumptions:

1. The reader has a need for information on outsourcing -- its advantages, disadvantages, and suitability for use in Government contract administration.
2. That the reader is in a position to use outsourcing or recommend its use as a means to meet mission goals in an effective and efficient manner.
3. That the reader commands a general knowledge or familiarity with Government contracting.

## **F. METHODOLOGY**

The methodology used in this thesis to answer the primary and subsidiary research questions are the following:

1. Conduct a comprehensive literature search of DoD directives, General Accounting Office (GAO) reports, business journals, magazine articles, internet articles and webpages dealing with the topics of outsourcing and inherently governmental functions.
2. Conduct site visits and face-to-face and telephonic interviews with the Commanders of DCMCs, to gain a thorough understanding of these DCMC

organizations, missions, resource constraints and functions and to gain insight into current and past outsourcing efforts.

3. Conduct face-to-face and telephonic interviews with industry representatives such as Brown and Root, Inc. and American Airlines to gain their assessment of the capability/ availability of outside sources for DCMC functions.

4. Conduct a site visit of the National Center for Policy Analysis in Dallas, Texas, to acquire literature on past cost benefit studies on privatization/ outsourcing efforts.

5. Conduct a survey of DCMC managers to gain insight into current DCMC outsourcing efforts.

## **G. ORGANIZATION OF THESIS**

This thesis is organized around five chapters. Chapter I provides an introduction and background, and outlines the objectives and research questions of the thesis. It establishes the framework and ground rules for the thesis in the scope, assumptions and methodology. Chapter II introduces the reader to the concept of outsourcing, provides a definition of privatization and outsourcing and states the advantages, disadvantages and current guidance related to outsourcing Government functions. Chapter III provides an overview of the DCMC organization. The mission and functions of DCMC will be discussed, both pre-award and post-award. The core functions of DCMC as specified by the FAR will be described. The concept of “inherently Governmental functions” will be defined and discussed and at this point, the functions performed by DCMC will be reviewed to determine which, if any, by definition, are inherently Governmental. Chapter IV will conclude with a look at which functions of DCMC are currently outsourced or have been outsourced and will conclude with a discussion of the results of market

research conducted to identify potential commercial sources of contract administration functions. Chapter V will provide data analysis. Chapter VI will provide the researcher's recommendations, conclusions and answers to the primary and subsidiary research questions. Specific recommendations are offered by the researcher as to whether DCMC should pursue an A-76 cost study to outsource its functions. Areas for further research are then identified and discussed.

## II. INFRASTRUCTURE REDUCTION AND OUTSOURCING

### A. BACKGROUND

The Fiscal Year 1998 National Defense Authorization Act directs the Secretary of Defense to submit to Congress an implementation plan to streamline the acquisition organizations, workforce and infrastructure. In his letter to Congress dated 01 April 1998, Secretary of Defense William Cohen provides a vision of an acquisition workforce that in the year 2008 is “smaller, and in fewer organizations; ... overseeing contracts to make sure the work gets done on time, with tough performance parameters, focused on managing suppliers rather than supplies.”[Ref. 7]

Pursuant to the requirements of the National Defense Authorization Act, Secretary Cohen announced a sweeping program to reform the business processes of the Department of Defense (DoD).[Ref. 8] The Defense Reform Initiative (DRI), essentially outlines a plan to mirror those business practices that American industry has successfully used to become leaner, more flexible and more competitive, in order to meet the Congressionally mandated 25,000 personnel cut by the end of Fiscal Year 1998. [Ref. 9] According to Deputy Secretary of Defense John Hamre, the DRI captures business reforms already underway in DoD and is DoD’s “most comprehensive effort to bring reform to the business side of the department.” [Ref 10] Secretary Cohen believes that the DRI will bring about the savings necessary to fund what he terms as the “Revolution in Military Affairs”, which includes the development and procurement of a new generation of information-based weapon systems needed to ensure American military superiority in the future. The DRI describes two “pillars” which will result in meeting the required savings goals; (1) the elimination of unneeded infrastructure; and (2) the



introduction of competition into the non-inherently Governmental functions performed by the DoD civilian workforce.[Ref 11]

This chapter will discuss the concept of DoD infrastructure, the definition and the applicability to contract administration functions. The use of competition in both private sector and Government will be discussed, along with the advantages and disadvantages of the potential result -- outsourcing. Finally the process of introducing competition into Government functions, or the A-76 process, will be discussed.

## **B. FORCE INFRASTRUCTURE**

In a speech made to the US Conference of Mayors, Secretary Cohen emphasized the need to reduce force infrastructure:

We have slashed our forces by 36 percent since the height of the Cold War, the defense budget has been cut by 40 percent but our base infrastructure has been trimmed only by 21 percent. We have far fewer submarines, but the pier space supporting them has not fallen accordingly. We have far fewer aircraft but we have not seen a corresponding decrease in air bases. The gap between force structure and infrastructure represents billions of dollars going to part of our organization that we don't need, the very same billions of dollars we need to maintain readiness and modernize our forces. If excess infrastructure isn't eliminated, your sons and daughters will face the future with weapons that are obsolete.[Ref 12]

Given that the Secretary of Defense points to "infrastructure" reduction as a means of freeing up funds for sustaining readiness and achieving force modernization, the researcher will attempt to define the term. The DRI defines "infrastructure" as the "fat surrounding military muscle." [Ref. 13] Former Secretary of Defense, Caspar Weinberger provides examples of entire commands or activities within DoD as "infrastructure" -- "day care centers; Defense Logistics Agency (DLA), which handles

contract administration; material warehousing; inventory control and transportation of supplies; and the Defense Accounting and Finance Service (DFAS), which manages payroll and budget.”[Ref. 1] DoD’s own official dictionary defines infrastructure in terms of physical assets; “all fixed and permanent installations, formations or facilities for the support of military forces.”[Ref. 13] Webster’s defines “infrastructure” as: “the underlying foundation, basic framework or substructure of an organization or system.”[Ref. 14] General (Ret.) Chuck Henry, former Commander of the Defense Contract Management Command (DCMC) refers to infrastructure in DoD in personnel and functional terms: “all those personnel, civilian or military, not carrying a rifle, manning a ship, or flying a plane, who provide support functions for those forces.”[Ref. 15]

In his book, *Structure in Fives*, organizational theorist Henry Mintzberg equates the military to a “machine bureaucracy.” [Ref. 16: p.18) Using the machine bureaucracy frame of reference, additional clarification can be discovered through Mintzberg’s insight into the functions and role of infrastructure. The basic organizational structure of a machine bureaucracy (Figure 2.1) consists of four components:

1. the strategic apex or management
2. the operating core
3. the technostructure
4. support staff or infrastructure

In the strategic apex are found those people charged with overall responsibility for the organization -- the Chief Executive Officer, president, pope, superintendent or commandant -- and all other top-level managers. Included here as well are those who

provide direct support to the top managers -- secretaries, executive assistants, etc. The strategic apex is charged with ensuring that the organization serves its mission, and also that it serves the needs of those in control or otherwise have power over the organization. Mintzberg points out that those in the strategic apex of the machine bureaucracy are concerned with the fine-tuning of their machine. As the reward system for those in the strategic apex is based on efficiency, they perpetually search for more efficient ways to produce their good or service, both in the public or private sector.

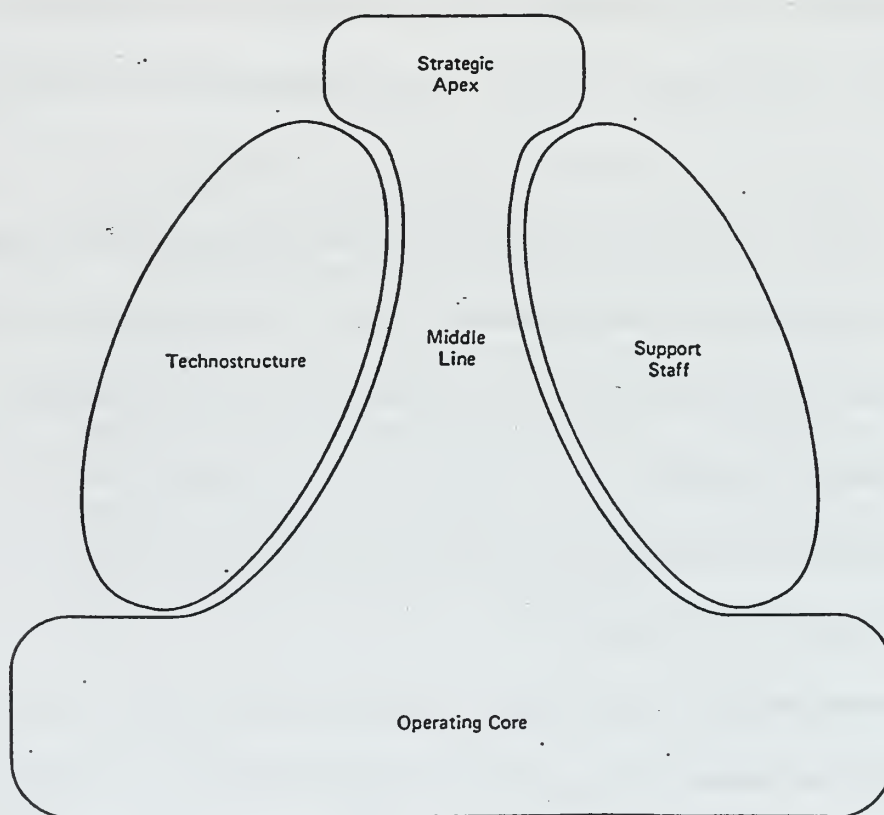


Figure 2.1  
Source: Mintzberg

The operating core of the organization consists of those people who perform the basic work related directly to the production of products or services. They transform inputs to outputs. Mintzberg refers to the operating core as the “heart of the organization,” [Ref 16, p.18] the part that produces the essential outputs to keep the organization alive. At a university, the operating core are those engaged in teaching and research. In a National Basketball League franchise, the operating core are those players in uniform and their coach. In a manufacturing firm operating core, Mintzberg includes plant managers, sales managers, foremen, machine operators, assemblers, salespeople and shippers.

The technostructure of an organization contains analysts and their supporting clerical staff, who serve the organization by affecting the work of others. These analysts are removed from the operating work flow -- although they may design it, plan it, change it or train the people how to do it. They help stabilize and standardize patterns of activity in the organization. In the manufacturing firm example, Mintzberg includes planners, the controller, training staff, operations researchers and production schedulers in the technostructure. Because the machine bureaucracy depends heavily on the standardization of its operating work processes for coordination, the technostructure -- which houses the analysts who do the standardizing -- emerges as the key component of the structure.

The support staff exists to support the other components of the organization and it is in this frame that Mintzberg identifies “infrastructure.” Mintzberg describes the support staff at a university as the personnel in the bookstore, printing shop, payroll department, janitorial service, mailroom, security department, purchasing department, athletics department, student residence and so on. None is part of the operating core, yet each exists to provide indirect support to the basic missions of teaching and research. In

the manufacturing firm, legal counsel, public relations, research and development, pricing, payroll, reception, mailroom and cafeteria all make up the support staff. In DoD, the support staff would include personnel performing many of the same functions as the examples above; purchasing, depot repair, housing, foodservice and payroll.

Given that the various definitions provided of “infrastructure” refer to either facilities, personnel or functions, for the purposes of this research, “infrastructure” is defined much as Mintzberg describes in the machine organization. The definition and description would include those personnel and facilities whose role it is to support missions carried out by operating military forces. The functions performed by this infrastructure includes such functions as; central acquisition of weapon systems, hardware and spares; contract administration; legal services; service record maintenance; payroll processing; invoice payment; foodservice; parts and material warehousing, inventory control and distribution; billeting; depot level (vice in the field) hardware maintenance; and quality of life services such as dependent health care clinics, commissaries, exchanges, day care centers and recreational facilities.

### **C. COMPETITION AND MARKET INFLUENCE**

For the purposes of this research, competition means simply putting Government services up for sale to the lowest bidder. Competition, to date, has had little application in Government, where monopolistic thinking has long prevailed.[Ref. 17] However, this mindset is changing. Of the DRI, Secretary Cohen states that we can expect increased competition through the A-76 process beginning in 1997, and points out:

We are going to compete with commercial activities. We should be competing many of the functions currently being carried out by Government employees. We will compete 34,000 full-time



equivalent positions in Fiscal Year 1998 and 120,000 positions over the next four years.” [Ref 11]

DoD has implemented various reform initiatives in the past to achieve efficiencies and reduce infrastructure costs. The Defense Management Review (DMR), Base Realignment and Closure (BRAC) process, National Performance Review (NPR), the bottom-up review and, more recently, the Defense Science Board (DSB) have identified similar problems with DoD’s support structure. All of these initiatives have pointed to competition as the centerpiece of their reforms to reduce infrastructure and create a Government that works better and costs less.[Ref. 18] The NPR of 1993 espoused the notion of requiring Government entities to compete with the private sector on a performance and cost basis as a means to better fulfill their missions. The NPR cited the Government Printing Office (GPO), the National Oceanic and Atmospheric Administration (NOAA), DoD, the General Services Administration (GSA) and the Federal Aviation Administration (FAA) as public activities, whose functions should be subject to increased competition.[Ref. 19] More recently, Deputy Secretary Hamre cited competition as a necessity in achieving the force reduction goals necessary into the 21st century:

We need to realize that the benefits of competition are not a luxury, but a necessity, as we seek to maintain the world’s premier military force as we enter the 21st century. Across the Department the question will be asked, “who can carry out defense support functions better, the government or the private sector?” [Ref. 10]

Business consultant and managerial professor William Halal points to internal competition as the new foundation of corporate management.[Ref. 20: p. 72] Progressive companies like Hewlett Packard, MCI, Johnson and Johnson, Asea Brown Boveri and



Alcoa which were traditional hierarchical organizations have become clusters of autonomous divisions. These divisions have their own distinct products, clients and competitors. At times they may sell to other divisions within the parent organization, compete against one another for the same customers, and even award contracts to outside competitors. According to Halal, the reasons are efficiency oriented:

These firms want to force the market into every nook and cranny of the firm. When hierarchical controls are replaced by market forces, the release of entrepreneurial energy produces the same self-organizing, creative interplay that makes external markets so advantageous -- solutions to difficult problems emerge far more quickly, permitting a rush of economic growth that can rarely be planned by even the most brilliant managers of hierarchical systems. [Ref. 20: p.72]

#### **D. INTRODUCING COMPETITION TO GOVERNMENT FUNCTIONS**

Office of Management and Budget (OMB) Circular A-76[Ref. 21] provides the procedure for subjecting Government functions to a bidding process. A-76 states that the Government will outsource all commercial activities, that is, those products and services which could be obtained from a commercial source, unless one of the following criteria is present:

- No commercial source is available to provide the product or service.
- The function must be performed in-house due to national defense reasons as certified by the Secretary of Defense.
- Direct patient care may be retained in-house if the agency's chief medical director determines it to be in the best interest of the patients.
- The Government can perform the function at a lower cost.
- The function is inherently Governmental. This will be discussed at length in a subsequent chapter.

The Circular delineates a process to be followed when considering outsourcing a Government function from in-house performance to contract (and vice versa). There are six basic steps:

1. The Government develops a detailed Performance Work Statement (PWS).

The PWS defines the tasks to be performed or provided, with performance standards and measures.

2. The Government develops a Most Efficient Organization (MEO) which will be the basis for the in-house cost estimate. The MEO is the Government's opportunity to reengineer and present a competitive structure. The MEO is considered procurement sensitive until bid opening or negotiations are completed.

3. The Government develops an in-house cost estimate for performing the function based on the MEO.

4. A Request for Proposal (RFP) or Invitation for Bid (IFB) based on the PWS is issued by a warranted contracting officer (CO). All competitive methods of procurement provided by the FAR are appropriate for cost comparison, to include sealed bid, two-step or negotiated procurement techniques. The CO must insert the clauses at FAR 52.207-3, which requires a contractor to give Government employees who have been adversely separated or impacted by the award of the contract the right of first refusal for employment openings in positions for which they are qualified.

5. All offers and proposals are compared against the in-house cost estimate. If discussions and negotiations are conducted with offerors the in-house cost estimate is compared against the final, most advantageous proposal. The personnel costs in the Government in-house estimate are automatically adjusted downward by ten percent for price comparison purposes. Based on the lowest price, the Contracting Officer announces the tentative winner, subject to possible appeals.

6. Appeals are considered by any interested party to the process, including Government employees. [Ref. 21]

This process is required if the outsourcing will involve ten or more employees, unless specific waivers to the process are granted.

## **E.      OUTSOURCING AND PRIVATIZATION**

While the use of privatization or outsourcing is increasing, the concept is not clearly or uniformly defined. Author Tom Shoop of Government Executive, states, “In the purest form, the term ‘privatization’ refers to the shifting of the production of a good or the provision of a service from the Government to the private sector, often by selling off government assets.” [Ref 23: p.18] The 1993 NPR took a rather narrow view; “When we talk about privatization, we don’t mean contracting out, we mean purely divesting.” [Ref. 24] Thus, for the purpose of this research, privatization is the transfer or divestment of not just the function, but in some cases also entire facilities to the private sector. The government agency is no longer responsible for that function, or for providing that service. An example of privatization would be the Department of Energy’s decision to sell off all land and rights of the Elk Hills Naval Petroleum Reserve in California to Occidental Petroleum in 1997.

The term “outsourcing” is defined as the basic decision of a Government agency to transfer the performance of tasks that were traditionally done in-house by Government personnel to either the private sector, or another Government agency. [Ref. 23: p.18] As opposed to privatization, when a Government function or task is outsourced, the Government remains fully responsible for the provision of the affected services, while another entity performs the function. [Ref. 25] For example, the Defense Contract Management Command (DCMC) provides Government-furnished property (GFP) management services as a contract administration service. DCMC may choose to outsource the personnel required to perform the tasks involved with property

management but DCMC would remain responsible for providing the service. Three examples of traditional outsourcing would be:

- The decision of Naval Fleet Imaging Center, Guam to contract out film-developing tasks in 1994.
- The Air Force deciding to close Newark Air Force Base, Ohio and privatize-in-place (PIP) its former depot-level repair of inertial guidance and navigation systems mission.
- The Army's decision to outsource all Base Operating Support (BOS) functions, which includes enlisted dining facility, public works, transportation, family housing maintenance, barracks management and personal property, as a Government-Owned-Contractor Operated (GOCO) contract with Brown and Root Services at Fort Huachuca in 1995. [Ref. 26]

Another form of outsourcing used in Federal Government is franchising, or cross-servicing, an arrangement where one agency provides support functions to another agency on a reimbursable basis. In 1993, the NPR encouraged agencies to get into the business of selling their services by establishing fully self-supporting units called "franchises." [Ref. 27] The NPR's goal was to reduce Federal overhead by cutting down on the cloning or redundancy of staff support functions in virtually every agency of the Government, by giving managers a choice in finding the best service value for the dollar. In 1994, the Government Management Reform Act (GMRA) established franchise funds for six agencies, providing working capital needed for planning and marketing. The range of franchised services proposed within these six funds ran the gamut of support functions, to include payroll and accounting, security, computer services, telecommunications, consulting, travel management, copying and printing, personnel management, health services and specialized training. [Ref. 17] Current examples of cross-servicing arrangements include NASA utilizing DCMC contract administration services on a reimbursable basis, the National Oceanographic and Atmospheric



Administration (NOAA) providing procurement and contract administration services to agencies outside of the Commerce Department and the Department of Justice and the Agency for International Development having their payroll processed by the Department of Agriculture's National Finance Center (NFC) in New Orleans. The NFC currently services more than 100 Federal agencies. [Ref. 28]

## **F. ADVANTAGES OF OUTSOURCING**

Outsourcing is common in the private sector as firms attempt to become leaner and more efficient, in other words, more profitable. [Ref. 17] The Outsourcing Institute [Ref. 29] compiled research to identify ten reasons why private firms choose to outsource some of their functions:

- **Improve Company Focus:** Outsourcing allows companies to free-up management time previously spent on non-core functions and refocus on meeting customer needs.
- **Resources not Available Internally:** Companies may outsource if they do not have the required resources in-house to meet an ongoing or new requirement.
- **Function Difficult to Manage:** Outsourcing allows companies to let experts from other firms manage their non-core functions.
- **Reduce Operating Costs:** Perhaps the single most compelling reason to outsource, lower cost structures lead to bigger profits.
- **Cash Infusion:** Often outsourcing involves the sale of assets to the provider, creating significant cash flow.

- **Free-up Capital Funds:** Outsourcing allows firms to reduce investment capital in non-core functions.
- **Free Resources:** An organization can refocus its people from unprofitable endeavors to more value-added activities.
- **Risk Sharing:** Companies outsource to become more flexible, dynamic and better able to meet changing opportunities.
- **Accelerated Reengineering Benefits:** Outsourcing allows companies to realize immediately any anticipated benefits of reengineering.
- **Access to World-Class Capabilities:** Just as clients have outsourced to improve their core business functions, vendors have focused their skills in their areas of expertise.

In a study titled “Leveraging Intellect,” [Ref. 30] researchers conclude that the best managed companies in the private sector increasingly focus on identifying and developing their core competency. Companies identify those functions that are most desired by customers, which the firm’s performance is best-in-world levels. If the company is not best-in-the-world at an activity, it gives up a competitive edge by performing that function in-house. [Ref. 30: p.12] By combining these core competencies with aggressive outsourcing strategies for non-core functions with “the world’s most effective external suppliers,” these companies become simultaneously the lowest cost, broadest line, most flexible and most highly differentiated producers in their markets. [Ref. 30: p.13] The specialized external suppliers in turn invest in their own core competencies, and acquire the best facilities and talent, for their own specialties. According to the researchers, no other strategy supports (a) efficiency (through focus), (b)



innovative flexibility (through multiple sourcing) and (c) stability (through market diversity) to the same extent. [Ref. 30: p.14]

Examples of companies with strategic outsourcing strategies include:

- MCI, which has only 1000 full-time technical people internally, yet has over 20,000 professionals working for it on contract basis. Besides outsourcing software, construction and system maintenance, MCI actively seeks out and exploits thousands of small firms to attach to its core software and electronic hardware.
- Boeing, which outsources many parts of its commercial airliners to those who have greater skills in specialized areas, retaining in-house portions of the craft that contain the critical flight control and power plant interfaces.
- 3M, which despite marketing over 50,000 products, historically rests its internal Research and Development (R & D) skills in only four core technologies; abrasives, adhesives, coatings-bondings and non-woven technologies, outsourcing R & D in other product lines. In each 3M has developed knowledge bases exceeding those of its competitors. [Ref. 30: p.14]

Former Deputy Secretary of Defense John P. White addressed the need to outsource additional Government functions currently performed in-house. During hearings before the Senate Armed Services Subcommittee, April 17, 1996, he stated:

The central focus of the outsourcing initiative is to maintain and improve our combat effectiveness. Outsourcing offers the opportunity to achieve that goal by generating savings for modernization, sustaining readiness, and improving the quality and efficiency of support to the warfighters. [Ref. 31]

In agreement with Dr. White, several research studies show that Government agencies have achieved cost savings and increased efficiency as a result of the

outsourcing process. A study by the Reason Foundation analyzed over 100 Government outsourcing efforts over the course of the last 20 years.[Ref. 32] These include Federal, state and local agencies. The functional areas included such services as legal services, payroll and data processing, printing service, property value assessment for tax purposes, welfare case work, air traffic control, port control, Naval tug service, elementary school teachers, weather forecasting, bus services, fire protection, refuse collection and privately run prisons. The study concludes that cost savings ranged from 20 to 50 percent as a result of outsourcing efforts. [Ref. 32: Executive Summary] It is important to note that the primary method of obtaining the cost savings stemmed from outsourcing to private firms, however increased competition also yielded cost savings by retaining the work in-house as a result of the MEO and from outsourcing to other Governmental agencies, similar to franchising agreements discussed earlier. Hilke concludes that however the function was outsourced, “All these benefits stem primarily from the introduction of competition into the bidding process to perform the service.”[Ref. 32: Executive Summary] The study pointed to a wide variety of reasons for the cost savings, including:

- Better and more productive equipment
- Better management techniques
- Greater incentives to innovate (profit factor)
- Incentive pay structures
- More efficient deployment of workers
- Greater use of part-time and temporary employees
- Utilization of comparative cost information

- More work scheduled for off-peak hours

In a study with similar results, the Center for Naval Analysis (CNA) examined 2,100 military outsourcing cases conducted between 1978 and 1994, and found that the outsourcing process, on average, saves 30 percent or \$1.5 billion in personnel costs, annually. Additionally, the CNA found that when private firms failed to win contracts in competition with civilian Government employees, which is the case in about half of A-76 comparisons, the MEO process still reduced costs by an average of 20 percent. [Ref. 33] Dr. Paul Kaminski, former Under Secretary of Defense (A & T) said of this study: “Let me repeat, our objective is to improve performance and lower costs, not replace Government workers with contractors.”[Ref. 2]

Similarly, economist Steven Rhoads studied the ability of Government to reap the rewards of increased efficiency on two recent studies:

1. One study compared Government and private performance of residential refuse collection. The study showed that, on average, US cities with over 30,000 residents get roughly 30 percent cheaper service when they hire firms to pick up refuse than when a city or county agency performs the work. Rhoads suggests that the difference stemmed from higher municipal absentee rates (12 percent vs. 6.5 percent), larger municipal crews (3.26 workers vs. 2.15), and the longer time it took the municipal crews to service each household (4.35 work hours per year vs. 2.37). [Ref. 34: pp. 69-71]

2. A second study by GAO found that it costs the Government nearly twice as much as it costs private insurance carriers to process each medical claim. The Government was also found to be slower in paying claims. The cost results were

explained by higher Government salaries and lower productivity. Despite higher wages, Federal employees processed an average of just 2,500 claims per year compared to 3,900 for Travelers, 4,200 for Mutual, 5,700 for Blue Cross of Maryland, and 6,600 for Blue Cross of Chicago.[Ref. 34: pp. 69-71]

Based on the results of the DRI, Secretary Cohen announced that 34,000 full-time equivalent (FTE) positions will see their functions competed with the private sector in FY98. Over 120,000 FTEs will be competed through the A-76 process through the year 2003. This represents a three-fold increase in the number of DoD FTEs competed in any previous year. Secretary Cohen estimates that DoD can achieve over \$2 billion savings annually from subjecting these FTEs to the competitive process. [Ref. 8] This estimate represents a 20 to 30 percent net cost savings.[Ref. 18]

Within DoD, there are hundreds of examples of where the outsourcing process has yielded service being performed better, cheaper and faster. Here are a few:

1. Subsistence Prime Vendor is an ongoing program outsourcing the DoD food procurement, storage and distribution functions completely to private industry. A single commercial distributor serves as the sole point of contact and provider of food products to DoD customers within a geographic region or zone. The contractor provides not only the products but also the storage and transportation of the merchandise. This is a significant departure from past practice when food for DoD facilities was centrally procured by Defense Personnel Support Center purchasing agents, through thousands of contracts with individual food wholesalers, stored in hundreds of DoD warehouses throughout the country and delivered by DoD personnel and vehicles.



The results of Prime Vendor have been three-fold: reduced infrastructure costs, improved service, and improved food quality. In the Jacksonville zone alone where the number of customers includes 22 ships and five shore-based dining facilities, DLA has been able to save an estimated \$2 million per year in overhead, based on contract costs through Beaver Street Foods. This cost included the cost of nine employees, including warehousemen, purchasing agents, and delivery drivers, the cost of operating two dedicated cold storage warehouses and three delivery trucks.[Ref. 35] Under the old system, a customer was required to submit his food order to a DoD supply center ten days prior to the desired date of delivery. Delivery times could not be guaranteed, and the average fill rate for the orders was 76 percent of the items ordered. Under Prime Vendor the vendor delivers within 48 hours of receiving the order and fill rates are running at 98 percent. The standard of quality seems to have translated to better food quality for DoD customers as well, without an overall increase in food costs. Since the conversion to Prime Vendor in 1994, the USS Leyte Gulf's estimated food costs are 6 percent below Government stock prices. [Ref. 36]

2. As stated earlier in this chapter, even when private firms do not win in direct competition with Government entities, the competitive process forces Government entities to adopt their Most Efficient Organization (MEO), yielding greater effectiveness and a cost savings of approximately 20 percent. [Ref. 32: Executive Summary] The Air Force estimates that by competing C-5 maintenance work with private firms, they realized a savings of 30 percent or \$190 million in personnel costs when they awarded a contract to Warner Robbins Air Force Base in Georgia in 1997. [Ref. 37]

3. The Army's Logistics Civil Augmentation Program (LOGCAP) contract is a mechanism whereby a contractor performs selected engineering and logistical services in wartime or contingency operations to augment Army forces. Currently LOGCAP is utilized for direct support of 27,000 US troops in the Bosnia UN peacekeeping mission. The services provided include the erection, operation and maintenance of base camps, the supply of fuel equipment and construction materials, foodservice, water purification, laundry, showers, sanitation service, vehicle repair, and transportation of personnel, mail and cargo. The contractor, Brown and Root, Inc., provides this service utilizing 6,766 personnel including both US and local nationals, for a contract price of \$458 million. The Logistics Management Institute (LMI) estimates that to provide the same services in-house, the Army would require 10,262 personnel at an estimated material and personnel cost of \$743 million. [Ref. 38] The researcher recognizes that the author of the LMI study, David Gallay, formulated his comparison based on the Army's Force Allocation Manning Doctrine along with the Army's deployment cost model rather than formulating a should-cost analysis for the comparison. [Ref. 39]

4. The Army transition program provides employment counseling service, including interview skills, resume writing and placement services for personnel transitioning from military to civilian life. Prior to 1990, the Army transition program consisted of a solely Government-staffed program serving over 100,000 personnel per year. The Army recognized that private corporations experiencing downsizing routinely provided similar services through contracted professional outplacement counseling firms. In 1991, the Army awarded a \$50 million Job Assistance Center contract to Resource Consultants, Inc. The result was a better and cheaper service than the Army was



performing with in-house assets. The Army realized a 35 percent decrease in Army unemployment insurance reimbursements to the department of labor, representing a savings of \$70 million per year. Soldiers who completed the new program achieved a starting salary \$7,500 per year higher than those who did not receive the services. Unemployment among Army veterans who participated in the program was one-half the rate of those who did not take advantage of the services. [Ref. 22: pp. 41-42]

## **G. DISADVANTAGES ASSOCIATED WITH OUTSOURCING**

While the current trend is towards outsourcing and privatization within DoD, “privatization is the most important defense management initiative of the post-Cold war period,” [Ref. 40] there are many potential pitfalls, in terms of combat readiness, financial realism and political fallout if wholesale privatization is pursued. The researcher has identified several pitfalls.

**1. Flaws and Inaccuracies Projected by A-76 Studies.** GAO has reported in several reports on prior A-76 competitions that the 30 percent savings reported are not reliable:

We have reported that (1) savings estimates represent projected rather than realized savings; (2) the costs of the competitions were not included; (3) baseline cost estimates were lost over time; (4) actual savings have not been tracked; (5) where audited, projected savings have not been achieved; and (6) in some cases work contracted out was more expensive than estimated before privatization. [Ref. 18]

Lt. Chris Luz performed an after-the-fact cost comparison of the outsourcing efforts at Naval Air Station, Fallon, NV. As a result of an A-76 study in 1987, most of the base support functions at Fallon were outsourced under one comprehensive contract, called Base Operating and Support (BOS). The BOS contract encompasses essentially

every support function previously performed by civil service or military personnel, including barracks management and operation, dining facility management, public works functions, electrical, vehicle and material handling equipment (MHE) maintenance, military housing maintenance, fuel farm and delivery, spare parts inventory, hazardous material handling, personal property services, servmart, runway and road maintenance, bomb range management, security, landscaping and pest control. Luz compared actual contract costs, including modifications, at Fallon for fiscal years 1993 through 1996 versus the costs for the same functions performed in-house at NAS Miramar for the same period. Luz' findings showed that of the nine cost centers studied at Fallon, only three showed actual cost savings, while the remaining six were "significantly cheaper to perform using in-house forces at Miramar." [Ref. 41]

NPR financial management team-leader, Michael Serlin, points to an inherent flaw in the process of competing Government functions with the private sector: "How do you establish a basis for comparing bids among entities that don't have common accounting practices, tax obligations or profit requirements?"[Ref. 17] A-76 competitions require the Government to include overhead costs in their in-house cost estimates. In a GAO study of 109 A-76 competitions, completed prior to 1996, the Government failed to include overhead rates in their in-house estimates.[Ref. 42] Of the 12 cases where the Government did include overhead rates, ten used rates of three percent or less. The Office of Management and Budget (OMB) and DoD officials questioned by GAO indicated that overhead rates were not included because they were "too difficult to quantify and allocate."

In 1996, after the private sector voiced concern that Federal agencies were not applying accurate overhead rates, leading to understatements of their proposed costs, OMB, after conferring with both Government and private sector representatives, revised the A-76 process and established a standard 12 percent overhead rate to be applied to all Government in-house cost estimates. GAO reports that the 12 percent rate is not based on empirical cost evidence, but rather is a midpoint of rates proposed to OMB. OMB, recognizing that the 12 percent rate does not fit all situations, allows agencies to calculate its own rate on a case-by-case basis. GAO further reports that given the complexity of establishing an independent overhead rate, and the fact that no adequate Government cost accounting system is in place, no agency has varied from the 12 percent rate. GAO concluded that had the Government applied the 12 percent rate to its in-house estimates prior to 1996, approximately one-third of the competitions won by the Government would have been won by the private sector. [Ref. 42]

**2. Need for Retaining a Competent “Core” Workforce.** Some in Congress stand against “wholesale” privatization. Representative Glenn Browder (D-Ala) emphasized a need to retain “a trained, reliable ‘core’ workforce, which owes allegiance to the government, not corporate executives.” [Ref. 43: p.20] According to Rep. Jim Hansen (R-Utah), whose district includes the Air Logistics Center in Ogden, Utah:

We see privatization in place as the first step towards a 100 percent private depot system, which would be a disaster for DoD. The services have a real requirement for a ready, controlled source of maintenance, because when it comes time for war, they can’t afford to start renegotiating contracts. [Ref. 44: p.43]

**3. Adverse Impact on People and Communities.** Nearly one-third of all Americans rely on Government for their sustenance. [Ref. 43: p.21] When the private

sector wins A-76 competitions, which they do in half the cases, Government employees can be adversely affected. According to one study by Army analyst Michael Brower, despite A-76 provisions that replaced civil servants have a “right of first refusal” on outsourced jobs, [Ref. 21] eight percent ultimately get involuntarily separated.[Ref. 43: p.21] According to Brower:

In private industry, with an upsurge in workload, a firm can easily hire more workers and with a lull in demand, easily lay them off. Workers, and their steady paychecks that they spend right on the economy, are less vulnerable in the Government. Attempting to give the taxpayer the best value for his dollar through outsourcing is a noble goal. However, when the majority of taxpayers are the very workers and voters injured in the process, it would be prudent for DoD to use caution and case-by-case consideration. [Ref. 43: p.22]

**4. Contingencies Create Cost and Performance Problems.** The customers of the BOS contract at NAS Fallon or Prime Vendor at DPSC have discovered the difficulty in crafting contract language to cover all conceivable contingencies. When an additional requirement within the scope of work is ordered, a modification must be written, usually increasing the contract price. [Ref. 41: p.31] This process can be both frustrating and costly to DoD managers. CDR Jim Souba, Public Works Officer at Fallon, states:

It is frustrating to look around and realize I don't have one guy in green to swing a hammer. Everytime an event occurs that is out of the ordinary, I have to modify the contract. I'm sure this (BOS) system is much more costly than before. I'd prefer the organic capability of having my own people. [Ref. 45]

As mentioned earlier in this chapter, the Subsistence Prime Vendor contract works effectively and efficiently at CONUS shore facilities. However, according to Capt. Paul Bland, Prime Vendor project officer, when faced with supporting troops stationed



overseas or any contingency requiring units to deploy, DLA must revert to the old organic subsistence resupply capability. This is because DPSC has not been able to craft and award a cost effective Prime Vendor contract to support deployed units in all parts of the world. Therefore, the full possible cost savings of eliminating stateside infrastructure is not yet realized. [Ref. 46]

**5. Current Vendor Capacity May Not Meet Outsourcing Needs.** In 1997 GAO studied the feasibility of outsourcing Government finance and accounting functions. [Ref. 28] As a comparison, GAO focused on 12 large companies who have pursued outsourcing. GAO found that while large organizations have been able to find vendors to outsource the most repetitive and labor-intensive portions of their finance and accounting functions, they could not find firms to take over the entire function. Three organizations found only one vendor capable of providing the breadth of service required, but only at non-cost-effective rates. According to GAO, the lack of a competitive marketplace for some DoD functions may adversely affect the cost savings projected by such studies as the DRI. [Ref. 28: p.10]

## **H. SUMMARY OF CHAPTER**

In this chapter, the researcher has provided background into mandated DoD FTE reductions called for in the 1998 National Defense Authorization Act. Per the Defense Reform Initiative (DRI), the required reductions will be realized through the reduction of unnecessary or excess force infrastructure and through the introduction of competition, through the A-76 process, in all non-inherently Governmental functions. Infrastructure was defined as those roles or job functions that are performed, by military or civilian personnel, to support missions carried out by operating military forces and includes the function of contract administration.

The process for introducing competition to Government functions--the A-76 process-- was introduced. The terms “outsourcing” and “privatization” were discussed and contrasted. The advantages of outsourcing Government functions to the private sector were identified as being lower costs and improved effectiveness. The disadvantages of outsourcing Government functions were identified as the loss of control over the workforce, the difficulty in accurately evaluating Government costs for the purpose of fair competition with the private sector, the adverse affect on communities and people, and the need to retain a competent core workforce in DoD in case of war.





### **III. CONTRACT ADMINISTRATION SERVICES AND INHERENTLY GOVERNMENTAL FUNCTIONS**

#### **A. CONTRACT MANAGEMENT AND ADMINISTRATION SERVICES**

##### **1. Goal of Contract Administration.**

The nature of Government purchasing mandates extensive pre-award and post-award contract oversight by the Government as a means of protecting the public interest. [Ref. 47: p.8] DoD buys from virtually every industrial segment of the economy-- research, development, services, construction, agriculture, energy, shipbuilding, automotive, transportation and aerospace. As such, Government purchasing is subject to complex laws and regulations; laws designed to fulfill multiple public policy objectives such as socio-economic programs. Many DoD programs require large industry investments in technology-driven work, requiring long-term business relationships. Often, when purchasing new technology, contract language requires substantial, direct pre- and post-award interaction between DoD and the supplier. Often DoD requirements are not well-defined, and require the use of incentive and cost-reimbursement types of contracts to mitigate performance risk on the supplier. The use of cost-reimbursement type contracts requires a greater level of buyer-supplier interaction and coordination during performance than firm-fixed-price contracts. [Ref. 47: p.9]

The Federal Acquisition Regulation (FAR) states that the goal of the Federal Acquisition System is to satisfy the customer in terms of cost, quality and timeliness. This performance standard is the responsibility of the Acquisition Team, consisting of representatives from technical, supply, procurement, customers and contractors.[Ref. 48] More specifically, on DoD contracts, the Acquisition Team consists of the end-user or

customer of the product, the program manager (PM) or user's representative, the Procuring Contracting Officer (PCO), the Defense Contract Audit Agency, the Defense Contract Management Command (DCMC), and the contractor. [Ref. 49: p.1] Author Stanley Sherman states that the goal of contract administration is to:

...ensure that performance by a supplier meets the objectives of the buyer, which are definable in terms of three categories of measurement -- performance, schedule and cost. These measurements are expressed with varying degrees of precision in the contractual arrangement. [Ref. 47: p.3]

## **2. Contract Administration Functions**

In DoD, upon awarding a contract, the PCO assigns responsibility for contract administration to a contract administration office (CAO). DCMC is the central CAO for DoD. The Federal Acquisition Regulation (FAR) states that the PCO shall retain contract administration responsibility if the contract requires performance on a military installation or at other than the contractor's facility. [Ref. 48: Part 42] Upon assignment of contract administration responsibility, the contract administration office (CAO) is required to perform 69 tasks normally delegated and 11 additional tasks that may be delegated by the PCO. Many of the 69 tasks require joint effort between the PM, PCO and CAO. According to Sherman, there are six broad categories of contract administration (CA) functions:

- **Monitoring and surveillance.** The objective here is to observe and acquire information concerning the contractor's compliance with contract provisions. To act as "eyes and ears" of the PM and PCO. This includes the monitoring of production progress and conducting compliance inspections of end items.

- **Reports and services to the PM, PCO and contractor.** This category includes regular or special administrative reports such as evaluation of contractors' requests for deviations, review of Value Engineering Change Proposals (VECP) and conducting pre-award surveys.
- **Reviews and audits of contractor's internal management systems.** This category includes compliance reviews of contractor systems and plans and includes Contractor Purchasing Systems Reviews (CPSR), quality assurance plans, compensation plan, insurance plan, drug-free workplace program, Cost Accounting Standards (CAS) and property accounting systems.
- **Formal decisions and actions affecting contractors.** These decisions are made by a warranted Administrative Contracting Officer (ACO) or the PCO based on information gathered from three categories above. Examples are determination of non-compliance with CAS, release of shipments from the contractor, notice of cost disallowance, approval of subcontracting plan and determination of final overhead rates.
- **Direction, negotiation and agreements.** This category involves interaction and negotiation between the contractor and Government to resolve problems, redirect efforts or to settle claims. It includes such tasks as negotiating pricing rates, billing rates, price adjustments, terminations and making administrative changes to the contract.
- **Program-sensitive contract management functions.** Sherman includes in this category all of the tasks already located in the above categories. The

reason they may be co-located in this category is that if the tasks may significantly impact cost, schedule or performance, the PCO or PM may want to retain significant visibility, control or involvement in the functions.

Table 3.1 places all 69 plus the 11 optional contract administration tasks into the first five of the six categories. Since the sixth category may contain any or all of the functions, it is omitted from this table.

## **B. DCMC MISSION AND ORGANIZATION**

### **1. DCMC Overview**

DCMC is DoD's central provider of contract administration (CA) services.

Established in 1990, the DCMC mission is to "provide customer focused contract management services throughout the acquisition lifecycle--around the clock--around the world." [Ref. 50] To accomplish its mission, DCMC employs 14,490 personnel.

Headquartered at DLA headquarters in Fort Belvoir, Washington, DC, DCMC personnel work at 81 different contract administration offices (CAOs). DCMC provides CA services on over 350,000 individual contracts valued at over \$111 billion. The 81 CAOs are divided among three district headquarters, District East in Boston, District West in El Segundo, Ca., and District International at Fort Belvoir. The individual CAOs are organized in one of two ways. DCMC area offices (AOs) are responsible for providing CA services for all contracts let with contractors within set geographic boundaries.

Examples of AOs are DCMC Springfield and DCMC San Diego. In-plant CAOs reside in or near large contractor facilities and provide CA services on all contracts let with that contractor. Examples of in-plant offices are DCMC Hughes in Tucson and DCMC Raytheon-TI Systems in Dallas.



<b>Task</b>	<b>FAR Cite</b>	<b>Performed by</b>
<b>Monitoring and Surveillance</b>		
Observing for appropriate restrictive markings	42.302(48)	1910/2032
Monitoring security requirements	42.302(20)	1102/1910
Monitor contractor industrial labor relations	42.302(34)	1102
Monitor compliance with contract provisions	42.302(40)	1910/1102/1103
Ensure notification IAW Limitation of Cost clause	42.302(15)	1102
Monitor production status/ progress	42.302(31)	1150
Conduct inspection of end-items	42.302(38)	1910
Observe contractor quality assurance tests	42.302(38)	1910
Monitor compliance with safety requirements	42.302(39)	1150/18
Monitor compliance with cost/schedule/performance on engineering design and development	42.302(40)	801/855
Monitor value engineering program	42.302(49)	801/855
Monitor flight test operations	42.302(56)	801
Monitor compliance with QA plan	42.302(38)	1910
Monitor compliance with small disadvantaged business and labor surplus area plans	42.302(54/55)	1102
<b>Reports and Services to PCO and Contractor</b>		
Conduct Post-Award Conference	42.302(3)	1102/1150
Assist contractor in acquiring tax exemption	42.302(18)	1102
Process duty-free certificates.	42.302(19)	1102
Assist with Priorities and Allocations (DPAS)	42.302(33)	1102
Administer advance payments	42.302(13)	1102
Manage special bank accounts	42.302(14)	1102
Provide technical review of contractor proposals	42.302(4)	1102/ 801/896
Gather cost/price data to prepare for negotiations	42.302(67)	1102
Conduct engineering reviews of cost proposals	42.302(44)	801/855
Observe and report faulty specs or technical documents	42.302(43)	1910/801
Evaluate and advise PCO on ECPs, VECs	42.302(45/46)	801/855
Evaluate request for deviations and waivers	42.302(47)	1102
Submit reports on progress and potential or actual delay	42.302(31/67)	1150/1102
Process and execute novation agreements	42.302(25)	1102
Conduct pre-award surveys	42.302(32)	1102/1150
Notify PCO when unilateral purchase order is rejected by contractor	42.302(63)	1102
Perform contract closeout activities	42.302(65)	1102
Screen, redistribute, and dispose of contractor inventory	42.302(28)	1103
Evaluate proposals for use of Govt. facilities	42.302(30)	1102/801
Review request for advance payment	42.302(12)	1102

Table 3.1 Functions of Contract Administration  
Source: Lackey interview and Moore Thesis

<b>Task</b>	<b>FAR Cite</b>	<b>Performed by</b>
<b>REVIEW AND AUDIT OF CONTRACTOR INTERNAL MANAGEMENT SYSTEMS</b>		
Review and audit of contractor maintenance, logistics and modification program	42.302(42)	1102
Conduct purchasing system review (CPSR)	42.302(50)	1102
Verify financial condition of contractor	42.302(16)	1102
Conduct audit and review of insurance practice	42.302(2)	1102
Review and assess value engineering program	42.302(49)	801
Review preservation and packing system	42.302(37)	2032
Review Govt. property accounting system	42.302(26)	1103
Review drug-free workplace program	42.302(66)	1102/1150
<b>FORMAL DECISIONS AND ACTIONS AFFECTING CONTRACTORS</b>		
Review and approve small disadvantaged business plan	42.302(52-53)	1102
Approve request for special test equipment	42.302(27)	1102
Approve request for advance payments	42.302(12)	1102
Review and approve subcontracting plan	42.302(51)	1102
Issue GBLs, releasing shipment of products	42.302(35)(60)	2100/2032
Determine final overhead rates	42.302(9)	1102
Determine allowability of costs	42.302(8)	1102
Determine adequacy of and compliance to contractor CAS disclosure statement	42.302(11)	1102
Approve/disapprove requests for GFP	42.302(26)	1102
Authorize non-contractual use of GFP	42.302(26)	1102
Issue decisions under the Disputes Act	42.302(10)	1102
<b>DIRECTIONS, NEGOTIATIONS AND AGREEMENTS</b>		
Issue work requests under maintenance and overhaul contracts	42.302(21)	1102
Make administrative changes to contract	42.302(59)	1102
Issue contract modifications	42.302(29)	1102
Negotiate prices for spares	42.302(22)	1102
Negotiate cancellation charges	42.302(24)	1102
Negotiate forward pricing rate agreements	42.302(5)	1102
Negotiate interim billing rates	42.302(67)	1102
Negotiate contract price adjustments	42.302(11)	1102
Negotiate advance agreements	42.302(6)	1102
Execute supplemental agreements	42.302(11,63,64)	1102
Negotiate termination settlements	42.302(23)	1102
Negotiate settlements for handling excess GFP	42.302(26)	1102
Negotiate price for contract modifications	42.302(67)	1102
Collect overpayments from contractor	42.302(17)	1102
Negotiate definitized price on unpriced orders	42.302(67)	1102

Table 3.1 Functions of Contract Administration (cont)

## 2. DCMC Staffing and Skills Requirements.

In order to meet their mission, DCMCs, whether in-plant or AOs, employ several different General Schedule (GS) job series personnel. The following is a typical array of GS workers who perform specific CA tasks at both in-plant and area CAO with a brief description of their duties and tasks. The source of the position requirements is the Handbook of Occupational Groups and Series. (Ref. 51) Table 3.1 displays which GS series performs specific CA tasks.

- **GS-801 General Engineering Series.** Professional engineering. Duties are to advise on, administer, supervise or perform research on: strength and strain analysis of materials such as elastic limits, maximum unit stresses, coefficients of expansion, workability, hardness, tendency to fatigue, resistance to corrosion, engineering adaptability, etc.
- **GS-855 Electronics Engineering Series.** Requires application of knowledge to advise, administer, supervise or perform research in areas of electronic circuits, circuit elements, communications, computation, sensing, control, measurement and navigation.
- **GS-896 Industrial Engineering Series.** Requires ability to analyze integrated systems of employees, materials and equipment, to ensure efficient production of a product or service.

- **GS-1102 Contracting Series.** Manages, supervises or performs work involving the procurement of supplies, services, construction, or research and development. Tasks include the preparation of requests for proposals, evaluation and analysis of contract price or cost proposals, negotiation, award, modification, termination and closeout of contracts. Requires knowledge of legislation, regulations, industry practices and sources of supply.
- **GS-1103 Industrial Property Management Series.** Requires a knowledge of business and industrial practices, procedures and systems for the management and control of Government-furnished property (GFP). Involves ensuring adherence to contract provisions regarding control of GFP from acquisition through disposal.
- **GS-1150 Industrial Specialist Series.** Evaluates and advises on the materials, methods, facilities used by an industry producing a commodity. Advises on plans for expansion, conversion, integration or utilization of industrial production facilities. Conducts surveys of industrial plants to evaluate capacity and potential for production. Evaluates production operations to optimize efficiency. Requires a knowledge of the nature and operations of an industry or industries and the facilities, methods and materials employed by that industry.

- **GS-1910 Quality Assurance Series.** Advises on quality of products and services acquired by the Government. Develops plans for assuring product quality and conformance to contract specifications. Requires analytic ability combined with knowledge and application of quality assurance principles and techniques, pertinent product characteristics and manufacturing processes and techniques.
- **GS-2130 Traffic Specialist Series.** Advises on, administers, supervises or performs technical work involving the provision of the most economical and efficient transportation of freight service to the Government. Requires a knowledge of transportation industry regulatory controls, the competitive practices of carriers, and a general knowledge of law, business management and economics.
- **GS-905 General Attorney Series.** Renders legal advice and services with respect to regulations, practices or other matters falling within the purview of a Federal Government agency. Drafts, negotiates, examines and makes recommendations concerning contracts. Makes recommendations for disposition of cases arising under contracts.
- **GS-018 Safety and Occupational Health Management Series.** Involves the management, administration, evaluation or operation of safety and occupational health activities. The objective of this work is the elimination or minimization of human injury and productivity losses. Requires knowledge



of the principles, standards and techniques of safety and occupational health standards.

- **GS-2032 Packaging Series.** Involves planning or evaluation of packaging methods, and directing or evaluation of packaging and packaging materials to protect supplies and equipment during shipping. Requires knowledge of methods and techniques to prevent environmental and mechanical damage.

### **C. DETERMINING LEVEL OF DCMC OVERSIGHT AND STAFFING**

In 1994, the DoD Inspector General (DoDIG) issued a report on DCMCs effectiveness and efficiency at planning, implementing, reporting and managing contract oversight. [Ref. 6] The DoDIG found that DCMC lacked an effective process for determining manpower requirements. The assignment of resources was found by DoDIG to be based on the availability of time and manpower, rather than a consideration of specific risks or of the customer's essential needs. Partly as a response to the DoDIG report, DCMC established the "One Book" in 1995. [Ref. 52: p.64] The "One Book" now provides DCMC managers a standard methodology for performing contractor risk assessment and for determining manpower requirements. Upon receipt of a contract for administration from the PCO, DCMC establishes a surveillance plan to determine the level of oversight required and the number of people required to perform the oversight functions. Largely, the plan and extent of surveillance is based on two criteria:

1. The criticality designator assigned by the PCO to the supplies or services, that is; an A (highest criticality level), B or C designator based on the Defense Priority System.

## 2. A risk assessment of the contractor and the requirement.

The risk assessment is developed jointly between DCMC and the PCO. The risk assessment addresses all facets of the contractor's ability to meet the terms of the contract including a review of:

- Past performance history of the contractor on both Government and commercial contracts.
- Maturity of the product design
- Contractor's financial capability
- Maturity of the contractor's production processes
- Evaluation of the contractor's production plan
- Commercial certifications achieved by the contractor such as ISO 9000

## **D. INHERENTLY GOVERNMENTAL FUNCTIONS**

### **1. Definition**

Inherently Governmental functions may not be considered for outsourcing under the A-76 program. [Ref. 21] GAO defines an "inherently Governmental function" as one that:

...is so intimately related to the public interest that it must be done by federal employees. These functions include those activities that require either the exercise of discretion in applying Government authority or the making of value judgments in making decisions for the Government. Government functions normally fall into two categories: (1) the act of governing, i.e., the discretionary exercise of government authority, and (2) monetary transactions and entitlements.[Ref. 25]

The Office of Federal Procurement Policy (OFPP) Policy Letter 92-1 [Ref. 53] establishes Executive Branch policy relating to service contracting and inherently Governmental functions. The letter provides an illustrative list of functions that are, as a matter of policy, inherently Governmental. According to OFPP, an inherently Governmental function is one that by the interpretation of the law and subsequent action:

- a. Binds the United States by contract, policy, order or otherwise;
- b. Determines, protects or advances the United States' economic, political or other interests;
- c. Significantly affects the life, liberty or property of private persons;
- d. Commissions, appoints or directs employees of the United States;
- e. Exerts ultimate control over the acquisition, use or disposal of property of the United States;
- f. Exerts ultimate control over the collection, control or disbursement of appropriated and other Government funds.

To further clarify the principle and criteria in determining whether a function is inherently Governmental and thus cannot be contracted out, GAO states:

The Government should not contract out its responsibilities to serve the public interest or to exercise its sovereign powers ...administration begins when the contractors involvement in basic management functions is so extensive than an agency's ability to develop options other than proposed by the contractor is limited. [Ref. 54]

OFPP states that inherently Governmental functions do not normally include gathering information or providing advice, opinions, recommendations or ideas that assist Government officials, who are ultimately accountable to the President, in making

informed independent decisions. Thus, a contract may be awarded where the contractor does not have the authority to decide on a course of action to be pursued but rather, is tasked to develop options to inform a Government official.

## **2. Functions Considered to be Inherently Governmental.**

The following is an illustrative list of functions considered to be inherently Governmental per OFPP [Ref. 53]:

- The direct conduct of criminal investigations.
- The control of prosecutions and performance of adjudicatory functions.
- The command of military forces, especially combat or combat support forces.
- The conduct of foreign relations and determination of foreign policy.
- The determination of agency policy, including the content of regulations.
- The determination of Federal program priorities or budget requests.
- The direction and control of Federal employees.
- The direction and control of intelligence and counter-intelligence operations.
- The selection of individuals for Federal employment.
- The approval of position descriptions and performance standards for Federal employees
- Determining disposition of Government property.
- In Federal procurement with respect to contracts:
  - determining requirements.
  - participating as a voting member on any source selection board.
  - approval of any contractual documents which define requirements.
  - awarding contracts.
  - administering contracts (including ordering changes in contract performance, quantities, accepting or rejecting contractor products or services).
  - terminating contracts.
  - determining allowability, allocability and reasonableness of costs.
- The approval of Freedom of Information Act requests.
- The determination of eligibility for a security clearance.
- The approval of Federal licensing actions and inspections.
- The determination of budget policy, guidance and strategy.
- The collection, control and disbursement of fees, taxes, fines, other than the collection of fees or fines at mess halls, post or base concessions, national parks, where the amount to be collected is predetermined.
- The control of treasury accounts.
- The administration of public trusts.



In addition to the functions specified by OFPP, GAO provides a list [Ref. 54] of additional functions that are considered inherently governmental as a result of laws or court decisions:

- The drafting and preparing of responses to Congress and testimony. (Comptroller General opinion in GAO B-237356, Dec. 29, 1989)
- Resolving disputes, compromise claims, terminate collection actions and initiate legal action. (Comptroller General 366, 1984)
- The operation and maintenance of Army Corps of Engineers hydroelectric power plants. (P.L. 101-640)

### **3. Functions Not Considered to be Inherently Governmental**

The following is an illustrative list of functions not considered to be inherently

Governmental per OFPP:

- Services that involve or relate to budget preparation, to include workload modeling, fact finding efficiency studies, and should-cost analysis.
- Services that relate to reorganization and planning activities.
- Services that relate to analysis, feasibility studies, and strategy options to be used by Government personnel in developing policy.
- Services that involve or relate to the evaluation of another contractor's performance.
- Services that involve or relate to the development of regulations.
- Services in support of acquisition planning.
- Services providing technical evaluation of contractor's proposals.
- Assistance in the development of statements of work.
- Services providing support in preparing responses to FOIA requests.
- Working in a situation that permits access to classified or sensitive information.
- Providing information regarding agency policies on behalf of the agency.
- Participating in a situation where it might be assumed that they are agency employees or representatives.
- Providing technical opinion on source selection boards.
- Participating as a voting member of a source evaluation board.
- Serving as an arbitrator or providing alternative methods of dispute resolution.
- Providing inspection services.
- Providing legal advice and interpretations of regulations and statutes to government officials.
- Providing security services such as prisoner detention or transport, and non-military national security details.



#### **4. DCMC Functions Considered Inherently Governmental**

Based on the CA functions performed by DCMC as listed in table 3.1, the following fit the OFPP definition of inherently Governmental:

##### **A. Actions Ordering or Authorizing Changes in Contract Terms or Performance**

1. Issuing work requests under maintenance and overhaul contracts.
2. Making administrative changes to the contract.
3. Issuing contract modifications.
4. Executing supplemental agreements.
5. Terminating Contracts.
6. Execution of novation agreements.
7. Issuing decisions under the Disputes Act.

##### **B. Approval of Required Systems, Plans or Programs**

1. Approval of contractor's purchasing system as result of CPSR.
2. Approval of subcontracting plan.
3. Determine adequacy of Cost Accounting System.
4. Determine adequacy of drug-free workplace program.
5. Determine adequacy of value engineering program.
7. Determine adequacy of property accounting system.
8. Determine adequacy of preservation and packing system.
9. Determine adequacy of Government property accounting system.

##### **C. Determining Disposition of Government Property**

1. Authorizing contractual or non-contractual use of GFP.
2. Issue duty-free certificates.
3. Issue GBLs, releasing shipment of products.
4. Approval of requests for special test equipment.
5. Redistribution and disposal of inventory.
6. Acceptance of end-items.

##### **D. Collection, Control or Disbursement of Funds.**

1. Collect overpayments from contractors.
2. Authorizing advance payments.
3. Manage special bank accounts.
4. Determine allowability or unallowability of costs.
5. Determine final overhead rates.

The above mentioned functions fit the GAO definition of inherently Governmental functions as “the exercise of discretion in applying Government authority or the making of value judgments in making decisions for the Government.”[Ref. 25]

## **IV. OUTSOURCING CONTRACT ADMINISTRATION FUNCTIONS**

### **A. INTRODUCTION**

This chapter will examine current, past and future outsourcing strategies at the Defense Contract Management Command (DCMC). Additionally, this chapter explores contract administration (CA) methods utilized in the commercial world as well as unique practices among other Federal agencies. And finally, the results of market research conducted to identify private firms who perform CA functions similar to DCMC, will be discussed.

In order to assess the current outsourcing efforts at the Defense Contract Management Command (DCMC), as well as to initiate market research into the existence of commercial suppliers of contract administration (CA) functions, a survey of 31 managers within DCMC was conducted. Of the 31 surveys issued, 21 responses were received. The survey questions were provided to commanders, deputy commanders and operations group leaders at DCMC area offices (AOs) and in-plant offices, as well as a former Commander, DCMC, the current deputy commander and the current director for contract management policy. The surveys were distributed either by electronic mail or personally by the researcher via face-to-face or telephonic interviews. A complete listing of those participating in the survey is provided in Appendix A. The questions posed in the survey are as follows:

1. Have you as a DCMC field manager (or at the headquarters/ system level) pursued outsourcing as a means to perform your organization's mission?
2. Have DCMC functions been put through the A-76 process?

3. Do you know if other DCMC components currently outsource or have outsourced CA functions in the past?
4. Have you been approached by, or are you aware of, companies who perform similar functions as DCMC?
5. If so, who are those companies?
6. Given the OFPP definition of “inherently Governmental,” and given the functions of contract administration provided by the FAR Part 42, do you feel that any or all of the CA functions performed by DCMC could be outsourced?
7. Which CA functions do you feel could be outsourced?

#### **B. CURRENT OUTSOURCING EFFORTS AT DCMC**

Of the 20 responses to questions 1 and 2 received --**“Have you...pursued outsourcing as means to perform your organization’s mission”?** and **“Have DCMC functions ever been put through the A-76 process”?**--there was no indication that DCMC currently utilizes outside agencies or private firms to perform CA functions. None of the respondents indicated that they had witnessed an A-76 study at DCMC. One respondent acknowledged that minor office or clerical work in the form of temporary hires to augment a DCMC contract administration office (CAO) during surge periods or computer support services, in support of the DCMC office, had been outsourced in the past. Another response revealed that DCMC Baltimore had hired a firm to conduct contract closeout functions in the distant past, but that the situation was not the result of an A-76 study, but rather a contract to support a surge period. The respondent could not recall who the company was. Ms. Jill Pettibone, Director of Contract Management Policy at DCMC, states:

No, we do not outsource contract administration functions. As you know we can't outsource inherently Governmental functions. Some people interpret that broadly and some narrowly. In the OFPP definition, contract administration is listed as inherently Governmental...the whole ball of wax. Under this construct, nothing can be outsourced. Other people believe that only decisions are inherently Governmental...which means everything up to the decision could be outsourced. [Ref. 55]

### **C. CONTRACTOR SELF-OVERSIGHT**

Although no survey responses indicated use of third-party outsourcing at DCMC, two survey responses did, however, indicate that DCMC is currently utilizing outsourcing in the form of a contractor self-oversight program. This program allows a contractor who is bidding on a contract to also propose a plan to conduct surveillance functions that would ordinarily be conducted by DCMC personnel on that contract.

As mentioned in Chapter I, in 1994 the Deputy Under Secretary of Defense (Acquisition Reform) directed that a cross-functional process action team (PAT) be formed to include representatives from the office of the Secretary of Defense (OSD), the Military Departments and DCMC. The PAT was to develop a specific plan of action to describe current inefficiencies in the DoD contract administration process and provide recommendations to resolve those inefficiencies. One of the specific recommendations was that DCMC should establish pilot locations to test the use of contractor self-oversight (CSO).[Ref. 6]

This PAT recommended that DCMC establish pilot locations to study the viability of using contractor employees as DCMC designees to perform quality assurance and production monitoring functions on behalf of DCMC on specific contracts. These designees are employees of the Government contractor, volunteered by the



company to be trained by DCMC, at contractor expense, to perform many of the same production and quality surveillance functions traditionally performed by DCMC personnel.[Ref. 56: p.1] The employee is dual-hatted in that he observes or performs the same quality assurance and production processes and end items, using the same measurement tools, as if he were a DCMC employee, yet he is an employee of the contractor. The self-oversight program is modeled after the Federal Aviation Administration's (FAA) technical compliance designee program, under which the FAA trains and certifies employees of aviation industry firms as FAA inspectors.[Ref. 6] The FAA's TCD program is discussed later in this chapter.

When a contract is let under the self-oversight plan, the contractor's personnel (TCDs) perform quality, production and GFP surveillance functions in lieu of DCMC personnel. The results of the 16 pilot programs indicate that, since contractors were already performing many of the same quality assurance tests currently conducted by DCMC, many duplicate DCMC tests and checks were eliminated.[Ref. 57]

Raytheon Electric Systems is one of 16 contractors to participate in the pilot tests. Raytheon produces the Advanced Medium Range Air-to-Air Missile (AMRAAM) on behalf of the Air Force, Navy and foreign customers, from plants in Arizona, Massachusetts and Pennsylvania. The scope of the oversight pilot included all AMRAAM products, including domestic and foreign missiles, spares hardware, pre-planned product improvement development and field return repairs. Raytheon personnel, trained and designated by DCMC, performed all quality assurance, production surveillance and GFP administrative functions including process audits, witnessing of tests, production reliability acceptance tests, Material Review Board dispositions,

product surveillance, quality deficiency report tracking and corrective action, special test equipment certification, engineering change proposal review, schedule tracking, GFP tracking, compliance review and DD-250 preparation.

Twelve metrics were jointly established by Raytheon and DCMC in order to measure the overall effectiveness of the surveillance process. During the program, DCMC conducted spot checks on the surveillance processes utilized by the TCDs to verify that the surveillance proposal was being adhered to and to evaluate its adequacy. For the self-surveillance program to be considered successful, the following criteria had to be met [Ref. 56: p.2]:

- Quality: AMRAAM product quality levels are maintained or improved during the pilot period.
- Cost: A reduction in total operating costs can be demonstrated during the pilot experiment as compared to the traditional DCMC oversight.
- Customer Satisfaction: The level of satisfaction with the process and DCMC services by the program office and field activities is maintained or improved.

According to Steve Titunik, deputy manager of DCMC Raytheon, all quality and customer satisfaction metrics on AMRAAM have been maintained or improved, while the program is saving DCMC one man-year per year in cost.[Ref. 58] Commander Fred Schellhammer, Commander of DCMC Pittsburgh, also states that utilizing contractors' personnel for ensuring contract terms are met results in significant manpower savings for DCMC with no degradation in quality.[Ref. 59]

As a result of AMRAAM and similar pilot projects, DCMC has recognized that training and certifying contractor personnel is a feasible oversight strategy for performing quality assurance, production surveillance and property management. In policy letter 98-05, DCMC headquarters advises its field activities that self-oversight proposals may be requested on all contracts where there is mutual consent amongst the CAO, the customer and the contractor.[Ref. 60] However, contractor personnel are not allowed to perform inherently Governmental functions such as acceptance of products or approving deviations.[Ref. 60] CAOs are permitted to use self-oversight proposals if the following conditions are met:

- Contractors must have an approved Government property control system.
- The contract administration office (CAO), contractor and all affected customers must be in agreement to use the self-surveillance approach.
- The CAO and the customer have confidence in the contractor's ability to provide the required surveillance and where the use of contractor surveillance will not result in additional cost or risk to the Government.
- The contractor agrees to enter a one year memorandum of agreement (MOA) acknowledging that regardless of surveillance arrangements used, the Government retains all rights under the inspection, property and other clauses of the contract.
- The quality, product and manufacturing surveillance plans are modified to indicate which processes or tasks will be performed by contractor personnel and how the CAO will ensure that the contractor is providing adequate assurance.

#### D. OPINION ON OUTSOURCIBILITY OF DCMC FUNCTIONS

In response to the question, “**Given the OFPP definition of “inherently Governmental and given the functions of contract administration provided by the FAR Part 42, do you feel that any or all of the CA functions performed by DCMC could be outsourced?”**”, 15 of 16 survey respondents stated that DCMC functions could be outsourced. Only one respondent stated that DCMC functions cannot be outsourced due to being inherently Governmental. Mr. Joe Thrailkill of DCMC Cincinnati states:

As you watch the activity of the private sector, you can observe the outsourcing of virtually every kind of business task. On that basis, practically every business function that DoD contract management offices perform could be done by the private sector.[Ref. 61]

In response to the question, “**Which CA functions do you feel could be outsourced?”**”, the respondents provided the following list of functions:

- quality assurance
- production surveillance
- pre-award surveys
- safety compliance
- engineering analysis
- plant and property clearance
- property management
- product acceptance
- transportation
- packaging
- flight operations

## E. COMMERCIAL CONTRACT ADMINISTRATION PRACTICES

To determine the latest commercial practices for performing CA functions, the researcher conducted surveys and interviews with buying offices of five companies, who do business with DoD, but none exclusively with DoD. All five companies have had DCMC personnel, either from in-plant resident or area offices perform CA functions on their products or services. The participating companies were:

- Planet Products
- American Airlines
- Halliburton
- Mentor Corp.
- General Electric Engines Division

Through interviews, these companies' representatives were asked the following questions:

- **What methods do you employ to ensure your company receives conforming goods from your suppliers?**
- **Do you use third-party pre-shipment inspection or quality assurance services?**

In every case, these companies, like DCMC, do spend some time in their suppliers' plants inspecting end-items. However, with in-house quality assurance inspections costly to the contractors, alternative methods of ensuring they receive a quality, conforming product, in lieu of source inspections, have been developed. Three strategies emerged from the interviews:



1. **Incentive of Continued Business.** All of the buyers interviewed state, in various degrees, that the best and most efficient quality assurance approach is the inherent knowledge on the part of the supplier, that failure to deliver a conforming, quality product on time, at a good price guarantees a loss of business in the future. Mr. Dan Thompson, contract manager for American Airlines (AA) states that AA's long-term CA plan is the Supplier Excellence 2000 program (SE 2000). The SE 2000 program is an agreement with key suppliers which promises that AA will conduct long-term business with the supplier provided the supplier demonstrates continuous, measurable improvement in price, quality and delivery. American may spend considerable time at the contractor plant observing manufacturing and quality assurance processes prior to award of national contracts. After award of a contract AA relies on the incentives of SE 2000 to ensure cost, performance and delivery requirements are met.[Ref 62] Major General Chuck Henry, former Commander of DCMC, told the researcher:

The question shouldn't be "can we reduce DCMC costs by outsourcing their functions." The question should be "why do we need a DCMC?" If we acted like smart businesspeople, we would stop doing business with companies who rip us off, and then we wouldn't need a DCMC. [Ref. 15]

2. **Reliance on Industry Quality Assurance Certifications.** General Electric (GE) Engines Division in Cincinnati relies heavily on suppliers who have achieved ISO 9000 or 9001 quality assurance certification. By contracting

with certified vendors, GE has been able to reduce the in-house costs of performing on-site product compliance tests.[Ref. 63]

3. **Use of Third-Party Inspection Services.** All of the firms interviewed have utilized third-party companies, either full-time or on a case-by-case basis to perform various CA functions, including quality assurance, engineering review, production cost surveillance and transportation control. Three scenarios emerged from the interviews in which these companies determine that third-party CA proved to be a wise business decision:

- **When administrative costs are too high or resources are lacking due to small company size.** Paul Stelmack, a buyer for Planet Products Corp. in Cincinnati states that outsourcing quality assurance services makes good business sense for his company; when internal buying and compliance costs are very high, for example, if we have to send an inspector across the country to inspect an item, outsourcing the inspection process may help hold the bottom line, if the service can be outsourced at a reasonable cost.[Ref. 64]
- **When a company lacks in-house technical expertise for the product being purchased.** Diane Calhoun, a buyer for Mentor Corp. in Irving, Texas, states that the decision to outsource makes sense in circumstances where technical knowledge of new or complex products is required and that knowledge is limited in her company. “We rely on laboratory services from companies like Chemir/ Polytech

for identification of materials, product contamination, comparative analysis of materials, failure analysis and quality assurance.”[Ref. 65]

- **When purchases are low in value or from a low-risk supplier.** In cases where the supplier is ISO certified, firms like GE still use independent testing firms like Accutek to perform periodic pre-shipment failure analysis, fatigue and QA testing. They retain their own in-house CA capability for proprietary product development contracts or for QA on new or non-certified suppliers.[Ref. 63]

In similar research on this topic, author Anne Millen Porter found that 46 percent of firms surveyed outsource purchasing and/or CA functions. Porter identifies four reasons given by firms that choose not to outsource[Ref. 66]:

1. Belief that there is not the same loyalty from outside companies as with employees as an incentive to obtain the same quality or value.
2. Belief that their buyers have extensive knowledge of their company’s products and do not believe a third-party entity could have the same level of knowledge to adequately complete the CA transaction.
3. Belief that all buying and quality assurance functions must stay with managers who have a personal stake in the success of the organization.
4. Belief that outside QA firms often serve many masters. Unless a company provides enough business that the QA firm serves that client only, there is always a chance that during critical supply periods, others are competing for the QA firms time and services.

In addition to the above four reasons, the researcher encountered a fifth situation in which a company would not be willing to have a third-party inspect their products on behalf of a customer. Chris Heinrich, general counsel for Halliburton, stated that many services or products provided by his company are proprietary.[Ref. 67] Halliburton would be hesitant to have a potential competitor inspecting its management or production processes on behalf of the Government, regardless of any conflict clauses that may be added to the inspector's contract.

#### **F. CONTRACT ADMINISTRATION AND COMPLIANCE APPROACHES IN OTHER GOVERNMENT AGENCIES**

The researcher encountered two examples of unique contract administration strategies within the Federal Government:

##### **1. Technical Compliance Designees.**

The Federal Aviation Administration (FAA) is the element of the US Government with primary responsibility for the safety of civil aviation. One of the FAAs major functions is regulating civil aviation safety. The FAA issues and enforces regulations and minimum standards relating to the manufacture, operation, flight control and maintenance of aircraft. The FAA is responsible for the rating and certification of pilots, airports, air traffic control centers as well as manufacturers of aircraft and aircraft components. Without an FAA certification, pilots cannot fly, flight control towers and airports towers cannot operate and companies cannot sell aircraft or aircraft parts in the United States or abroad.

To perform the certification function among manufacturers, the FAA employs 200 civil service employees nationwide. [Ref. 68] The majority of the FAA's

certification work is conducted by over 1500 industry personnel designated as technical compliance designees (TCDs). These personnel are employees of the manufacturer, but are trained and qualified by the FAA for the role of certifier. The designees officially represent the FAA but their salary and FAA training is paid by their own company. They inspect and evaluate their own companies' designs and manufacturing processes, conduct end-item testing and observe first-flight prototype tests. They have the authority to issue FAA air-worthiness certificates for end items. The certification issued by the individual is every bit as official as with an FAA-issued certification. Jim Reeves, manager of FAA's Atlanta District office states:

If the TCD issues a certification and then that company is later found to be in violation of FAA standards, they stand to pay a severe civil penalty--sometimes enough to put them out of business. The incentive to keep their certification and uphold FAA requirements is simple--if they lose it--they can't do business. We have that hammer that DoD doesn't. In 25 years I've yet to see a company lose their certification.[Ref. 68]

Mr. Reeves also states that the FAA certifies commercial aircraft that are produced on the same production line as military aircraft. For example the Lockheed 382J is essentially the same as the C130. As an illustration of the efficiency of the TCD program, Mr. Reeves states: "In the Lockheed plant there are 75 full-time DoD (DCMC) personnel inspecting the C-130. We (FAA) have two personnel inspecting the 382J, and I guarantee the 382J can match the performance and safety record of the C-130." [Ref. 68]

## **2. Outsourcing Contract Administration to Commercial Firms.**

The U.S. Postal Service (USPS) utilizes Stanley Associates to perform all carrier certification and compliance services. Stanley, a firm of 400 personnel, pre-certifies



domestic land and air carriers and ensures compliance with USPS contract terms. [Ref. 72]

The Department of Energy (DOE) contracts out the operation of several nuclear power plants around the country. DOE then contracts with Brown and Root Services to provide oversight of the contracted services.[Ref. 67]

## **G. MARKET RESEARCH RESULTS**

The researcher has attempted to find commercial sources to perform DoD CA functions. The researcher used the survey of DCMC managers, interviews with five private company buyers and an internet search for companies who perform quality assurance and inspection services.

The researcher asked DCMC managers, **“Have you been approached by, or are you aware of, companies who perform similar functions as DCMC?”** and **“If so, who are those companies?”** The results of the survey were successful in that six different companies were identified that perform functions similar to DCMC. The researcher conducted interviews and surveys with five of these companies. The survey question was asked (after Table 3.1 was provided): **“Having reviewed the contract administration functions in the Federal Acquisition Regulation, do you feel your company could perform some or all of those functions on behalf of DoD buying offices?”** The companies identified by DCMC that participated in the survey were as follows:

- Stanley Associates, Alexandria, Va.
- Accutek, Inc., Cincinnati, Oh.

- Inspectorate, Houston, Tx.
- R.L. Townsend and Associates, Dallas, Tx.
- Chemir / Polytech Labs, Inc., St. Louis, Mo.

Every company surveyed felt that many of the CA functions outlined in the FAR were within their ability to perform on behalf of DoD on a nation-wide or local basis. Many of the CA functions are core competencies of these companies. Tim Barrett, owner of Accutek, states that his company currently performs mechanical testing, quality assurance, engineering analysis and special testing CA services on behalf of General Electric(GE) on subcontractors for GE's DoD contracts.[Ref. 69]

Mr. Spencer Hutchins, president of Intertek, and the former QA director for DCMC's western district, states that not only could he perform the same functions as DCMC, but he should be given the opportunity to compete for the service. Intertek also currently performs QA and value engineering analysis work on behalf of prime DoD contractors. Hutchins states:

More and more, companies hire us for our expertise in performing surveillance and pre-shipment product inspection. I feel that on behalf of the Government, we could perform any CA function short of final product acceptance.[Ref. 70]

Inspectorate is an international firm which conducts pre-shipment tests of manufactured equipment and petrochemical products for customers throughout the world. Inspectorate's client list includes DoD prime contractors, Halliburton and Brown and Root. Houston district manager Dudley Houghton states,

I guarantee we could provide a level of expertise that will ensure you get the product you want from any supplier in the world. If we

aren't staffed for a particular product we often outsource for the expertise on an as-needed basis.[Ref. 71]

## V. DATA ANALYSIS

This chapter will analyze the data presented in previous chapters. The researcher presents his observations on whether the data gathered and presented are sufficient to answer the research questions directly and, where the data collected lead to ambiguous conclusions, draw comparisons and contrasts between the Defense Contract Management Command (DCMC) and private industry or other Federal agencies.

### A. INFRASTRUCTURE

The researcher holds that identifying and defining DoD infrastructure is a prerequisite to considering outsourcing functions at DCMC because the 1998 Defense Reform Initiative (DRI) calls for reduced infrastructure by means of outsourcing. To establish a definition, the researcher gathered and presented data from existing DoD publications, conducted a survey of three DoD officials, looked at specific DRI language and cited Webster's dictionary. (Chapter II) From seven sources, four distinct definitions emerged. Three of the sources defined infrastructure in terms of functions which support warfighters; i.e., running day care centers, transportation and warehousing. One source cited physical assets of DoD, that is land, piers, equipment and buildings. Two sources stated that infrastructure consists of people, i.e., non-warfighters, lawyers and support staff. Another defined infrastructure as individual military commands within DoD, such as the Defense Logistics Agency, the Defense Finance and Accounting Service and the commissary and exchange system. One source offered that infrastructure included all physical assets, the people who run them and the functions they perform as comprising infrastructure. The language of the DRI speaks of infrastructure both in terms of physical facilities and the people performing the work functions within those

facilities. Based on these diverse points of view, the researcher observes that there is no DoD-wide, readily available or unanimously acceptable definition of infrastructure.

However, the DRI's vision is that by reducing current infrastructure levels, the resulting cost savings will fund future modernization of our weapon systems. The process espoused by the DRI for reducing infrastructure is the A-76 process. The A-76 process entails detailing a work function and allowing external suppliers to bid for the opportunity to perform that function, hopefully resulting in lower costs for receiving at least an equal amount of service. The A-76 process does not reduce the level of service, but rather allows proposals on performing those functions at a lower cost, that is, using fewer Government resources like money, people and/or physical assets. Since the function or service provided does not decrease through the A-76 process, but potentially the number of people and the amount of resources required are reduced, the researcher deduces that infrastructure, as it applies to the goals of the DRI, consists of people and physical assets whose role and purpose is to support the warfighter.

To establish whether the personnel or functions performed by DCMC fit the definition of infrastructure, the researcher discusses in Chapter II, Mintzberg's organizational theory which equates the military to a machine bureaucracy. Within the framework of the machine bureaucracy, all strategic decision making occurs in the strategic apex, all core work functions are performed by the operating core, process analysis and efficiency studies are performed by the technostructure personnel and the support functions are performed by the support staff.[Figure 2.1] In Mintzberg's model, the support staff exists to support the operating core of the organization and includes the function of purchasing. For DoD and in the context of this research, the details and



regulations on how to perform 80 CA functions are provided by the FAR, the same regulation which provides guidance on the procurement function. As presented in Chapter III, the majority of the 80 CA functions are performed by GS-1102 series personnel, contract specialists, the same series performing the procurement function. The CA functions routinely performed by DCMC may be, and often are, retained and performed by the PCO. Given that CA functions are governed by the same regulation as the pre-award procurement function, that the series personnel performing those CA functions also perform the procurement function, and that CA functions are often retained and performed by procurement offices, all lead the researcher to conclude that the tasks involved in contract administration are an element of purchasing. If CA functions are an element of purchasing, then by Mintzberg's model, they are part of infrastructure. The researcher therefore concludes that the functions performed by DCMC personnel are subject to the mandate of the DRI, that is they are subject to the A-76 competitive process, where otherwise eligible.

## **B. BENEFITS OF OUTSOURCING**

Two major studies covering 2,200 A-76 studies over a period of 14 years, and presented in Chapter II, indicate that, on average, the Government saves 30 percent or \$1.5 billion annually through A-76 outsourcing process, while generally maintaining or improving the quality of the service. Even when the Government agency wins the competition, which happens in roughly half of A-76 cases, 20 percent savings are realized. These savings result from the requirement that the Government agency develop and then maintain the most efficient organization (MEO) as a competitive proposal on A-76 competitions.

The data presented in Chapter IV reveal that the CA functions performed by DCMC have not been through an A-76 competition. Neither was there evidence in the 2,200 studies cited in Chapter II, that any CA functions have been through an A-76 MEO process. However, other Federal agencies have outsourced portions of the contract administration functions, albeit not through an A-76 process. As presented in Chapter IV, the FAA and USPS both outsourced functions defined as CA functions, and have realized significant efficiency and effectiveness improvement.

Chapter II presented examples of cases in which the A-76 process led to a decision to outsource particular functions. The cost savings that were eventually realized fell well short of predicted savings. GAO reports that in cases where the Government agency wins the A-76 competition, the savings are often misrepresented due to flaws in the Government's MEO cost estimates, or because the agency reverts back to its former organization and does not adopt the MEO. Primarily, GAO felt that the Government underestimates its costs due to understated overhead rates, thus overestimating future savings. However, the researcher observes that understating the Government's cost proposal understates the margin of victory for private firms and understates future savings. Secondly, when a function is outsourced, there are cases when it ends up costing the agency more. Chapter II presented the case of outsourcing at NAS Fallon where an after-the-fact study shows that it has been more expensive to outsource civil service functions there than would have been the case otherwise.

Based on the data, the researcher recognizes that A-76 competitions have resulted in cases of erroneous outsourcing decisions and mistated savings. However, the preponderance of data collected lead the researcher to observe that, in general, the A-76

process yields savings, and/or improved effectiveness, regardless of whether the function is outsourced or retained. Because the overwhelming majority of data suggest that the competitive process yields savings to the agency and the fact that other Federal agencies have realized savings from outsourcing CA functions, the researcher concludes that DCMC could benefit in terms of effectiveness and efficiency by subjecting its functions to the A-76 process.

### **C. INHERENTLY GOVERNMENTAL FUNCTIONS OF DCMC**

Chapter III presented the definition of “inherently Governmental function” as stated by Federal policy and confirmed by case law as one which:

- Binds the United States by contract,
- Directs employees of the United States,
- Exerts ultimate control over the acquisition or disposal of property,
- Exerts ultimate control over the collection, control or disbursement of Government funds.

Chapter III also provided the 80 CA functions performed by DCMC. Given the above definition of inherently Governmental functions, the researcher observes that 30 of the 80 CA functions are inherently Governmental, and thus, according to the Office of Management and Budget (OMB), cannot be outsourced. The following are examples of CA functions that are inherently Governmental and the characteristics of each that lead the researcher to conclude they are inherently Governmental:

- acceptance of goods on behalf of the Government, approval of requests for use of Government-furnished property (GFP), issuing Government bills of

lading (GBL). These actions have the affect of exerting ultimate control over the acquisition or control of Government property.

- determining the allowability or allocability of costs or collecting overpayments from contractors. These actions exert ultimate control of disbursement or collection, control or disbursement of funds.
- Approval of contractor's purchasing system, subcontracting plan or requests for deviation. Issuing decisions under the Disputes Act, making administrative changes to a contract, issuing contract modifications, and terminating contracts. These are actions that bind the Government by contract.

Conversely, 50 of the 80 CA functions do not meet the above definition of inherently Governmental because they do not bind the Government or exert control over funds or property. The following functions are specifically mentioned by OFPP Policy Letter 92-1 as functions which are not "inherently Governmental" and as such, the researcher concludes that they could be outsourced. The opinion surveys presented in Chapter IV support this conclusion. Additionally, the fact that other Federal agencies have outsourced these functions to the private sector serves to substantiate this position. Chapter III provides an illustrative list of CA functions that are not considered to be inherently Governmental based on OFPP guidance including:

- Providing technical and engineering review of contractor's proposals; gathering cost and pricing data in preparation for negotiations; evaluation and assessment of contractors' internal management systems such as drug-free



workplace program; value engineering program and purchasing system; and participating as voting members of source evaluation boards.

- Observing end-item quality assurance tests, monitoring compliance with QA plans, conducting pre-award surveys and monitoring compliance with subcontracting plan.
- Preparing responses to FOIA requests, conducting post-award conferences, evaluation of requests for waivers or deviations, reviewing requests for advance payments.

#### **D. CONTRACTOR SELF-OVERSIGHT**

Chapter II provides a definition of outsourcing as a decision by a Government or private organization to have specific functions performed by another external organization. In the Federal Government, the process for determining if a function should be outsourced is the A-76 process. By utilizing contractor self-surveillance, as DCMC does on the Contractor Self-Oversight (CSO) program, discussed in Chapter IV, DCMC allows the contractor to perform the quality assurance, production surveillance and Government-furnished property management functions normally performed by DCMC personnel. Although the decision to utilize contractor personnel vice DCMC personnel to perform CA functions is not the result of A-76, the researcher nonetheless concludes that this program meets the definition and intent of outsourcing. The researcher observes that based on the cost/ benefit analysis of the sixteen self-oversight pilot programs as well as opinion from DCMC managers on current projects, that the self-oversight program demonstrates that CA functions can be successfully outsourced,



reducing DCMC manpower requirements, while not jeopardizing contract delivery schedules or quality.

**E. SOURCES OF SUPPLY FOR CONTRACT ADMINISTRATION FUNCTIONS**

The researcher conducted market research via survey, literature and internet search and personal interviews to learn of firms able and willing to perform CA functions similar to those performed by DCMC. Chapter IV presented five companies who currently perform inspection, manufacturing and engineering analysis and quality assurance functions on behalf of their clients. All five companies have clients that are DoD prime contractors, and the services they provide match closely those performed by DCMC. All managers interviewed were familiar with the role of DCMC and the CA functions listed in FAR Part 42. One of the companies, Stanley Associates performs quality assurance and supplier surveillance services on behalf of USPS. As presented in Chapter IV, all of the companies expressed an ability and a willingness to perform CA functions on behalf of DCMC. Because the market research yielded companies familiar with the CA functions outlined in the FAR, willing to perform those functions on behalf of the Government, and having demonstrated the capability to perform, the researcher observes that there are sources of supply for outsourcing CA functions.

## VI. CONCLUSIONS AND RECOMMENDATIONS

### A. SUMMARY OF RESEARCH

As presented in Chapter I, since the end of the Cold War, the number of Department of Defense (DoD) operating forces has been cut by 36 percent and the defense budget cut by 40 percent. However, DoD infrastructure has been reduced by only 21 percent in that timeframe. Infrastructure has been defined as functions performed by either military or civilian personnel to support missions carried out by operating military forces. As discussed in Chapter II, Secretary of Defense Cohen has declared that DoD must accelerate the reduction in infrastructure--and divert the funds required to maintain that infrastructure--in order to modernize our operating forces into the 21st century. The dilemma faced by DoD managers, including managers at the Defense Contract Management Command (DCMC) is that despite reduction in funding and manpower since the end of the Cold War, the scope of their missions and workloads have not necessarily decreased at the same rate as their resources. DoD managers are faced with developing new and innovative approaches to performing their missions in the face of reduced resources. This study has explored different DoD activities' use of outsourcing as a means to accomplish their mission more efficiently and effectively.

Outsourcing was defined as the transfer of workload, but not the responsibility for that work, from a DoD activity to either: (1) the private sector or (2) another Government agency. Secretary Cohen said in the Defense Reform Initiative that outsourcing is the pillar for reducing infrastructure, and creating a leaner, more effective DoD. Through the DRI, Secretary Cohen has put forth the mandate that 120,000 civil service positions will be competed via the Office of Management and Budget Circular A-76 (A-76) process

through the year 2002. Various functions will be put up for sale to the lowest bidder as a means to reduce infrastructure.

Past and current efforts to outsource contract administration (CA) functions efforts at DCMC and other Government agencies have been explored. Since functions that are “inherently Governmental” cannot be outsourced, the researcher has attempted to define “inherently Governmental” and explore if the definition applies to the functions performed by DCMC. Advantages and disadvantages of outsourcing, both in the private sector and in Government, have been discussed. Examples of outsourcing contract administration in three Federal agencies who have outsourced has been provided. Additionally, a DCMC pilot program for allowing contractor self-oversight has been explored.

## **B. CONCLUSIONS**

### **1. Conclusion #1**

**There is no consensus for a common definition of “infrastructure”.** Given that Secretary Cohen and other former Secretaries of Defense have called for the reduction of infrastructure along with the reduction of force size, the researcher attempted in Chapter II to find commonality in the various definitions. Of seven different sources of a definition, infrastructure was inclusively defined as either physical objects, people, an organizational pattern or a category of functions. For the purposes of establishing a common workable definition, the researcher defines infrastructure as personnel and facilities whose purpose it is to support missions carried out by operating military forces.

### **2. Conclusion #2**

**Personnel performing functions of contract administration (CA), as detailed in Chapter III, fall within the definition of DoD infrastructure.** As such, DCMC personnel performing the functions included in contract administration are included in the vision of the DRI which calls for 120,000 positions to be put through the A-76 process by the year 2002. Through Mintzberg's model, the researcher has demonstrated that all personnel whose job it is to support the operating core of the organization, are infrastructure.

### 3. Conclusion #3

**Savings achieved through the outsourcing process are not always the result of awarding a contract to a private enterprise.** The outsourcing process saves the military an average of 30 percent or \$1.5 billion annually in personnel costs. Both the Center for Naval Analysis and the Reason Foundation studies, presented in Chapter II, concluded that in the A-76 competitive processes completed since 1978, the Government agency wins half the time. The process of developing and maintaining the most efficient organization (MEO), and then winning in competition with private industry, yields a 20 percent savings.

### 4. Conclusion #4

**Outsourcing does not always result in savings.** Chapter II presented information that shows the cost savings projected by A-76 studies have been misstated due to several reasons, including: savings reported were based on projected, vice real, savings; the cost of the A-76 studies was not included in the savings calculation; outsourcing contracts require additional Government oversight and expensive modifications; and flawed Government overhead cost estimating procedures.

## 5. Conclusion #5

**Thirty of the 80 CA tasks performed by DCMC fit the definition of “inherently Governmental” and as such, cannot be outsourced.** As discussed in Chapter III, an inherently Governmental function is one which:

- Binds the United States by contract,
- Directs employees of the United States,
- Exerts ultimate control over the acquisition or disposal of property,
- Exerts ultimate control over the collection, control or disbursement of Government funds.

Given this definition, the researcher concludes that CA functions which are inherently Governmental include those functions which:

- Provide approval on behalf of the Government. For example: approval of the contractor’s purchasing system, subcontracting plan or requests for use of Government-furnished property (GFP).
- Control the disbursement or the collection of Government funds. For example: issuing Government bills of lading (GBLs), Determination of the allowability or allocability of costs or collecting overpayments from contractors.
- Directions, decisions or agreements which contractually bind the Government. For example: issuing decisions under the Disputes Act, making administrative changes to a contract, issuing contract modifications, acceptance of goods on behalf of the Government, and terminating contracts.

## 6. Conclusion #6



**Fifty of the 80 CA tasks performed by DCMC do not fit the definition of “inherently Governmental” and as such, could be outsourced.** Several responses to the survey discussed in Chapter IV indicated that only decisions that actually bind the Government, either by a Contracting Officer, or through ultimate product acceptance are inherently Governmental. The survey indicated that the majority of the surveillance, quality assurance, evaluation, fact-finding, property management and compliance review functions performed by DCMC could be outsourced. Chapter III provides an illustrative list of functions that relate directly to CA functions that are not considered to be inherently Governmental including:

- Services that include fact-finding and should-cost analysis, for example: providing technical and engineering review of contractors proposals; gathering cost and pricing data in preparation for negotiations; evaluation and assessment of contractors’ internal management systems such as drug-free workplace program; value engineering program and purchasing system; and participating as voting members of source evaluation boards.
- Services that involve evaluation of contractors’ performance or inspection service. For example: observing end-item quality assurance tests, monitoring compliance with QA plans, conducting pre-award surveys and monitoring compliance with subcontracting plan.
- Services providing support in responding to contractors’ requests. For example: preparing responses to FOIA requests, conducting post-award

conferences, evaluation of requests for waivers or deviations, reviewing requests for advance payments.

## 7. Conclusion #7

### **Contractor self-oversight is a viable method of outsourcing DCMC**

**functions.** The success of the 16 pilot programs indicates that outsourcing can reduce DCMC manpower requirements, while not jeopardizing contract delivery schedules or quality. As discussed in Chapter IV, DCMC has authorized system-wide use of self-surveillance where its use will not increase cost, schedule or performance risk to the Government. Contractor self-oversight should be used with contractors who have a proven record of satisfactory performance, with mature cost, schedule and quality assurance systems. The decision to use the CSO program has not been a result of the traditional A-76 studies.

## 8. Conclusion #8

### **Other Federal agencies have successfully outsourced their contract**

**administration functions.** The Federal Aviation Administration (FAA), the Department of Energy (DOE) and the US Postal Service (USPS) all currently outsource all or a part of their CA requirements. The technical compliance designee (TCD) program of the FAA is similar to the contractor oversight program in that, a company's own employees provide surveillance on behalf of the Government. DOE outsources the surveillance function over contractors who operate nuclear power plants. USPS utilized third party inspectors to monitor the performance of independent carriers.

## 9. Conclusion #9

There are several firms who claim to be able and willing to perform the same contract administration functions on behalf of DCMC. Chapter IV presented five companies who currently perform inspection, manufacturing and engineering analysis and quality assurance on behalf of clients that are DoD prime contractors. Two of the owners interviewed by the researcher are former DoD quality assurance personnel. All of the managers interviewed were familiar with the role of DCMC and the CA functions listed in FAR Part 42.

## C. RECOMMENDATIONS

### 1. Recommendation #1

The Secretary Of Defense should include the functions performed by DCMC as part of DoD infrastructure described by the DRI and thus, subject those non-inherently Governmental functions performed by DCMC to the A-76 competitive process. The DRI calls for over 120,000 civil service positions to be introduced to the competitive process over the next four years. To date, functions at DCMC have not been subjected to the A-76 process. The DRI advocates using best practices and lessons learned from leading-edge companies to reduce infrastructure. Leading private sector firms in search of leaner, more efficient and cost-effective organizations are increasingly outsourcing non-core functions or at least requiring internal business units to compete with external suppliers.

### 2. Recommendation #2

DCMC should adopt an outsourcing strategy which mirrors the goals of the DRI. DCMC management has been faced with the challenge of meeting a straight-line five percent per year manning reduction since 1990, and now faces a 25 percent

workforce reduction by the end of fiscal year 1998. However, DCMC's workload has not been reduced by the same percentage. In the same timeframe, 1990 to 1997, DCMC has seen the average number of contracts requiring oversight decrease by only 2.3 percent annually. Although DCMC has developed innovative means to accomplish its mission in the face of reduced resources, outsourcing through A-76 studies has not been one of those means. The A-76 process has been shown to produce savings of an average of 30 percent for Government agencies, without a degradation in quality.

### 3. Recommendation #3

**DCMC should conduct pilot A-76 studies on non-inherently Governmental functions, at one or more contract administration offices (CAO).** The A-76 process requires Government agencies to develop a most efficient organization (MEO) in preparation for the competitive process. The Government wins half of A-76 competitions, and the resulting MEO, if adhered to, achieves an average savings of 20 percent. Many of DCMC's functions are inherently Governmental and thus can be subjected to the A-76 process. There are companies that have expressed an interest and displayed an ability in competing for the right to perform CA functions. Other Government agencies have successfully outsourced CA functions.

### 4. Recommendation #4

**DCMC should expand the scope and use of the contractor self-oversight to include training and certification of contractor technical compliance designees (TCDs).** The FAA has achieved a noteworthy safety and quality record with minimal staffing through the use of TCDs as certifying officials. The contractor self-oversight program has proven to be an effective means of reducing DCMC surveillance manpower

without degradation in product quality. The contractor self-oversight program could be expanded to designate TCDs within companies, much like the FAA who could perform the same surveillance and inspection function as DCMC on all of the company's DoD contracts rather than specific contracts. The decision to designate company TCDs should be made with the same careful risk assessment and concurrence with buying offices as is required with contractor self-oversight.

## **D. ANSWERS TO RESEARCH QUESTIONS**

This section will discuss the primary and subsidiary research questions posed in Chapter I. All of the questions can be answered fully.

### **1. Primary Research Question**

**Can the CA functions performed by DCMC field offices be differentiated so as to identify those functions that can be outsourced?**

The functions performed by DCMC can be differentiated to determine the feasibility of outsourcing. As presented in Chapter 3, the 80 CA functions fit into five broad categories:

- Monitoring and surveillance
- Reports and services to the Program Manager, PCO and contractor
- Reviews and audits of contractors' internal management systems
- Formal decisions and actions affecting contractors
- Directions, negotiations and agreements



The Federal Acquisition Regulation (FAR) provides a comprehensive list of 80 CA functions which may be assigned to DCMC. To determine if a function can be outsourced, a determination as to whether or not the function is inherently Governmental must be made. The FAR, along with the DCMC “One Book,” provides sufficient details as to how to perform the tasks. The A-76 circular provides a clear, concise definition of functions that are inherently Governmental to allow a determination as to the legality of outsourcing CA functions. DCMC CA functions that are not considered to be inherently Governmental include:

- Services that include fact-finding and should-cost analysis, for example: providing technical and engineering review of contractors proposals; gathering cost and pricing data in preparation for negotiations; evaluation and assessment of contractors’ internal management systems such as drug-free workplace program; value engineering program and purchasing system; and participating as voting members of source evaluation boards.
- Services that involve evaluation of contractors’ performance or inspection service. For example: observing end-item quality assurance tests, monitoring compliance with QA plans, conducting pre-award surveys and monitoring compliance with subcontracting plan.
- Services providing support in responding to contractors’ requests. For example: preparing responses to FOIA requests, conducting post-award conferences, evaluation of requests for waivers or deviations, reviewing requests for advance payments.

## **2. Subsidiary Research Questions**

### **a. What is “outsourcing” and “privatization”?**

Privatization is the transfer or divestment of not just a Government function, but in some cases also entire facilities to the private sector. The Government agency is no longer responsible for that function, or for providing that service. An example of privatization would be the Department of Energy’s decision to sell off all land and rights of the Elk Hills Naval Petroleum Reserve in California to Occidental Petroleum in 1997.

Outsourcing is the transfer of the performance of Government tasks that were traditionally done in-house by Government personnel to either the private sector, or another Government agency. As opposed to privatization, when a Government function or task is outsourced, the Government remains fully responsible for the provision of the affected services, while another entity performs the function.

### **b. What is the process for determining if a function should or can be outsourced?**

The Office of Management and Budget (OMB) Circular A-76 delineates a process to be followed when considering outsourcing a Government function from in-house performance to contract (and vice versa). There are six basic steps:

1. The Government develops a detailed Performance Work Statement (PWS), defining the tasks to be performed with performance standards and measures.
2. The Government develops a most efficient organization (MEO) which forms the basis for the in-house cost estimate.

3. The Government develops an in-house cost estimate for performing the function based on the MEO.
4. A Request for Proposal (RFP) or Invitation for Bid (IFB) based on the PWS is issued by a warranted contracting officer (CO) to all interested bidders including other Federal agencies.
5. All offers and proposals are compared against the in-house cost estimate. The personnel costs in the Government in-house estimate are automatically adjusted downward by ten percent for price comparison purposes. Based on the lowest evaluated price or best value, the Contracting Officer announces the tentative winner, subject to possible appeals.
6. Appeals are considered by any interested party to the process, including Government employees.

This process is required if the outsourcing will involve ten or more employees, unless specific waivers to the process are granted. Inherently Governmental functions, as defined by OMB Circular A-76, cannot be subjected to the A-76 process.

**c. What are the advantages and disadvantages of outsourcing?**

Both Government agencies and private sector firms have pursued outsourcing as a means to become leaner and more efficient. As presented in Chapter II, advantages gained by DoD through outsourcing include an average of 30 percent reduced operating costs, increased effectiveness and more efficient use of resources.

Disadvantages of outsourcing DoD functions include:

- The potential for more costly performance by contractor than DoD due to inaccuracies in DoD's cost-estimating systems;
- The need to retain a competent core workforce in case of war;
- The adverse affect that outsourcing can have on people and communities;
- The costliness of issuing contract modifications in case of contingencies;
- Lack of vendor base to ensure adequate competition.

**d. What are “inherently Governmental functions?”**

As discussed in Chapter III, an inherently Governmental function is one which (1) binds the United States by contract, (2) directs employees of the United States, (3) exerts ultimate control over the acquisition or disposal of property or (4) exerts ultimate control over the collection, control or disbursement of Government funds.

**e. What functions currently performed by DCMC fit the definition of “inherently governmental?”**

CA functions which are inherently Governmental include those functions which:

- Provide approval on behalf of the Government. For example: approval of the contractor's purchasing system, subcontracting plan or requests for use of Government-furnished property (GFP).
- Control the disbursement or the collection of Government funds. For example: issuing Government bills of lading (GBLs), determination of the allowability or allocability of costs or collecting overpayments from contractors.
- Directions, decisions or agreements which contractually bind the Government. For example: issuing decisions under the Disputes Act, making

administrative changes to a contract, issuing contract modifications, acceptance of goods on behalf of the Government, and terminating contracts.

**f. Does DCMC currently subject its functions or personnel to the competitive A-76 process or have they in the past?**

There was no indication that CA functions or personnel at DCMC had ever been through the A-76 process. However, the contractor self-oversight program is a viable method of outsourcing DCMC functions. The research indicates that DCMC does not currently utilize outside agencies or private firms to perform CA functions, other than the current self-surveillance program. Only minor office or clerical work in the form of temporary hires during surge periods or computer support services, in support of the DCMC office had been outsourced in the past.

**g. Do other Government agencies outsource CA functions?**

The Federal Aviation Administration (FAA), the Department of Energy (DOE) and the US Postal Service (USPS) all currently outsource all or a part of their CA requirements. The technical compliance designee (TCD) program of the FAA is similar to DCMC's self-surveillance program, in that a company's own employees provide surveillance on behalf of the Government. DOE outsources the surveillance function over contractors who operate nuclear power plants. USPS utilized third party inspectors to monitor the performance of suppliers. To the tertiary question, "Does DCMC currently outsource?", one can argue that DCMC's contractor self-oversight program is a form of outsourcing without calling it by that specific word.

**h. Are there commercial suppliers for any or all of the DCMC functions?**



There are several firms who claim to be able and willing to perform CA functions on behalf of DCMC. Five companies who currently perform inspection, manufacturing and engineering analysis and quality assurance on behalf of clients that are DoD prime contractors and who expressed an interest and willingness to perform CA functions on behalf of DoD include:

- Stanley Associates, Alexandria, Virginia
- Accutek, Inc., Cincinnati, Ohio
- Inspectorate, Houston, Texas
- Townsend and Associates, Dallas, Texas
- Chemir / Polytech Labs, Inc., St. Louis, Missouri

#### **E. AREAS FOR FURTHER RESEARCH**

During this study, the researcher found three areas that warrant further research:

1. A cost-benefit analysis of the air-worthiness certification process employed by the FAA could provide DoD an alternate oversight model. As discussed in Chapter IV, the majority of the FAA's certification work is conducted by over 1500 technical compliance designees (TCDs). The TCDs are employees of private aviation firms, but are trained and qualified by the FAA for the role of certifier. The TCDs officially represent the FAA but their salary and FAA training is paid by their own company. They inspect and evaluate their own companies' designs and manufacturing processes, conduct end-item testing and observe first flight prototype tests. These individuals

have the authority to issue FAA air-worthiness certificates for end items. The certification issued by the TCD is every bit as official as with an FAA-issued certification. The FAA certifies commercial aircraft that are produced on the same production line as military aircraft. In the Lockheed plant where the 382J and C-130 are produced, there are 75 full-time DCMC personnel inspecting the C-130 and two TCDs inspecting the 382J.

2. Further research is required on the CSO program to determine if true manpower or cost savings have resulted. The researcher is concerned that the initial 16 pilot programs discussed in Chapter IV could have been hand-picked to ensure success. Now that DCMC has authorized the use of CSO for all programs, a random after-the-fact review, using actual cost data, may provide better analysis.
3. As presented in Chapter II, OFPP has issued guidance that when preparing a cost estimate for the Government MEO in the A-76 process, a flat 12 percent overhead rate should be applied. GAO concluded the 12 percent rate was not based on actual cost data but rather represents a best "estimate" of across-the-board overhead for all Federal activities. GAO concludes that this rate mistates actual costs, that each agency has different overhead costs and the basis for award on A-76 competitions is being made based on erroneous Government numbers. A study and compilation into actual overhead rates for each Federal, DoD or individual Service branch could serve as an accurate

cost estimator for A-76 competitions, increasing the likelihood that the true lowest bidder wins the competition, all other factors considered.

4. A potential barrier to outsourcing CA functions to a commercial provider is unwillingness of the prime contractor to allow third-party access to its processes and records. The researcher encountered a situation in which a company would not be willing to have a third-party inspect their products on behalf of a customer. As presented in Chapter IV, Chris Heinrich, general counsel for Halliburton, stated that many services or products provided by his company are proprietary. Halliburton would be hesitant to have a potential competitor inspecting their management or production processes on behalf of the Government, regardless of any conflict clauses that may be added to the inspector's contract. Further research should be conducted into the willingness of DoD contractors to have potential competitors providing oversight on behalf of the Government.

...the most common type of plagiarism is the use of words or phrases without acknowledgment of the source. This is often done in the form of a list of references at the end of a paper, but the references are not used in the text. This is a serious violation of academic integrity and can result in a student being charged with plagiarism. The student in this case was charged with plagiarism and was given a failing grade for the course. The student's defense was that the references were not used in the text, but the professor argued that the references were used in the text and that the student had not acknowledged the source. The student was found guilty of plagiarism and was given a failing grade for the course.

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## **APPENDIX: SURVEY QUESTIONS AND RESPONDENTS**

### **DCMC SURVEY QUESTIONS**

**The following questions were distributed to 31 DCMC management personnel via E-mail, phone conversation or face-to-face interviews.**

1. Have you as a DCMC field manager (or at the headquarters/ system level) pursued outsourcing as means to perform your organization's mission?
2. Have DCMC functions been put through the A-76 process?
3. Do you know if other DCMC components currently outsource or have outsourced CA functions in the past?
4. Have you been approached by, or are you aware of, companies who perform similar functions as DCMC?
5. If so, who are those companies?
6. Given the OFPP definition of "inherently Governmental", and given the functions of contract administration provided by the FAR Part 42, do you feel that any or all of the CA functions performed by DCMC could be outsourced?
7. Which CA functions do you feel could be outsourced?

### **The following individuals responded to the survey:**

Gen Chuck Henry, USA (Ret)  
Former Commander  
Defense Contract Management Command (DCMC)

Gary Thurber  
Deputy Commander  
DCMC

Jill Pettibone  
Executive Director, Contract Management Policy  
DCMC



Col. Frank Davis, USA  
Director of Acquisition Strategy and Privatization  
DCMC

LCOL John Heib, USAF  
Director, Flight Operations  
DCMC

Capt. Bruce Feehrer, USN  
Commander, DCMC Hughes Tucson

COL Anthony Love, USA  
Commander, DCMC Atlanta

CDR Dan Ryan, USN  
DCMC Hughes Tucson

LCOL Paul McQuain, USA  
Commander, DCMC Raytheon TI

Col. David Mastin, USA  
Commander, DCMC General Electric Aircraft Engines

Joe Lackey  
DCMC Raytheon TI Systems

CDR Fred Schellhammer, USN  
Commander, DCMC Pittsburg

LCOL. C. Mihok, USAF  
Commander, DCMC Stratford

LCOL Mark Brown, USA  
Commander, DCMC Clearwater

Thomas Lopez  
Deputy Commander, DCMC Stratford

Joe Traillkill  
Deputy Commander, DCMC General Electric Aircraft Engines

John Grubbs  
Deputy Commander, DCMC Atlanta

LCOL Greg Miller  
Commander, DCMC Seattle

Joe Caldwell  
Operations Manager, DCMC Lockheed Martin, Atlanta

Frank Toda  
Operations Group Leader, DCMC General Electric Aircraft Engines

Jeff Mason  
Deputy Commander, DCMC Raytheon TI Systems



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